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Technical Director
Financial Accounting Standards Board
401 Merritt 7
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Re: File Reference No. 1820-100

## **Dear Technical Director:**

On behalf of the National Association of College and University Business Officers (NACUBO), we submit the following comments on the proposed Accounting Standards Update, "Revenue Recognition (Topic 605): Revenue from Contracts with Customers" (the ASU). NACUBO's comments on the proposal were developed with input from our member institutions and our Accounting Principles Council (APC). The APC consists of experienced business officers from various types of institutions who, collectively, possess a thorough knowledge of higher education accounting and reporting issues and practices.

NACUBO is a nonprofit professional organization representing chief financial and administrative officers at more than 2,100 colleges and universities. In its capacity as a professional association, NACUBO issues accounting and reporting guidance for the higher education industry and educates over 2,000 higher education professionals annually on accounting and reporting issues and practices.

## **Overall Observations of the ASU**

The proposed guidance leaves open many questions about how not-for-profit organizations (NFP's) would apply the principles to their unique revenues. In the case of colleges and universities, it is unclear how revenue from research projects and tuition – two major sources of revenue – would be recognized under the ASU. In particular research projects which can stretch over many years and have only vaguely defined deliverables. In 2009, independent higher education institutions recognized over \$17 billion of sponsored research revenue and expenditures, with indicators of growing volume through 2010 and 2011.

Revenue generated from research is currently recognized in one of three different ways. The most common, especially for government sponsored research, is to record revenue as costs are incurred and billed. This is because the contract is for the performance of the research which is, in effect, being delivered as it is performed. Whether or not a report is issued to the sponsor at the end of the research project or at intervals throughout is incidental to the work that is being performed and for which the sponsor is paying. Other methods of recognizing research revenue include recognition costs billed on completion of milestones and predetermined payments, unrelated to costs incurred, recognized upon completion of milestones.

We are concerned that the guidance in the ASU does not adequately address this issue. An auditor may conclude that it is the reporting of the results to the sponsor that constitutes the performance obligation and, in that case, it could literally be decades before revenue could be recognized.

The ASU seems focused on entities that manufacture a product or provide a service such as consulting. The research undertaken by universities does not neatly fit into either of these categories. Nor is it always clear whether a particular institution gets a research contract because only it can perform the research or for a variety of other reasons making it difficult to determine if it is "distinct."

Finally, given the fact that this is a FASB and IASB jointly proposed standard, we request that NFP's be scoped out as the Boards have not included them within the scope of the convergence project. NFP's are unique in their activities and the revenues that they derive from those activities have clearly not been considered in the drafting of the ASU.

Rather than respond to each question in the ASU, we have selected those that reinforce our general observations and comments.

Question 2: The Boards propose that an entity should identify the performance obligations to be accounted for separately on the basis of whether the promised good or service is distinct. Paragraph 23 proposes a principle for determining when a good or service is distinct. Do you agree with that principle? If not, what principle would you specify for identifying separate performance obligations and why?

The guidance as to whether a good or service is distinct leaves significant room for interpretation and, as such, inconsistency in application. Again, with regard to research, there may not be a distinct or identifiable good or service that is being transferred. From the perspective of the researcher (vendor) it is the research itself. From the perspective of the sponsor (customer), however, it may be the results of the research once complete or unanticipated results along the way. For these types of contracts, we believe that the vendor should determine the criteria for determining when control passes to the customer.

Question 3: Do you think that the proposed guidance in paragraphs 25–31 and related implementation guidance are sufficient for determining when control of a promised good or service has been transferred to a customer? If not, why? What additional guidance would you propose and why?

We do not believe that the guidance, as written, is sufficient to cover all situations in which an organization must determine when control of goods or services passes to the customer. The criteria in paragraphs 25-31 does not sufficiently address long-term service contracts with deliverables that are not easily identified. In particular, those where the customer cannot direct the use of or immediately receive the benefit from the service – such as research projects.

Question 5: Paragraph 43 proposes that the transaction price should reflect the customer's credit risk if its effects on the transaction price can be reasonably estimated. Do you agree that the customer's credit risk should affect how much revenue an entity recognizes when it satisfies a performance obligation rather than whether the entity recognizes revenue? If not, why?

While we agree that a transaction price should be adjusted for a customer's credit risk, we are dubious as to the ease and accuracy with which such an amount could be reasonably estimated. In addition, we disagree with the Board's proposal that changes to the estimate be recorded as income or expense. Such changes should be recorded as revenue. To record them otherwise would be misleading to readers of financial statements who would not obtain the full picture of cash flows generated from revenue producing activities.

## Disclosures - Questions 10, 11 and 12

We strongly disagree with the proposed disclosures under the ASU. The proposed disclosures are excessive, onerous and potentially misleading to users of the financial statements. This is particularly true of those requirements that require forecasted or predictive information. Financial statements are meant to provide a snapshot of history, not be used as an oracle for the extent and timing of future transactions. Should this information be provided, it should be in an MD&A that has appropriate Safe Harbor provisions.

Additionally, we do not believe that the disclosure requirements are operational for organizations that have more than a handful of contracts. Many colleges and universities have thousands of contracts that would have to be analyzed in order to comply with the proposed guidance. To require the level of disaggregation suggested by the ASU would be potentially voluminous and provide little useful information to users. Any benefit would be far outweighed by the cost of providing such information.

Question 13: Do you agree that an entity should apply the proposed guidance retrospectively (that is, as if the entity had always applied the proposed guidance to all contracts in existence

during any reporting periods presented)? If not, why? Is there an alternative transition method that would preserve trend information about revenue but at a lower cost? If so, please explain the alternative and why you think it is better.

Retrospective application of the proposed guidance would be onerous. While we acknowledge that it would improve inter-period comparability, it would be extremely difficult to accurately apply the guidance to a prior year without significant work and analysis. Conversely, it would be equally onerous to provide pro-forma information reflecting amounts as they would have been presented prior to the implementation of the ASU.

Question 14: The proposed implementation guidance is intended to assist an entity in applying the principles in the proposed guidance. Do you think that the implementation guidance is sufficient to make the proposals operational? If not, what additional guidance do you suggest?

The examples provided in the implementation guidance are simplistic and not nearly encompassing enough to adequately assist in applying the principles in the proposed guidance. We would like to see more examples related to the delivery of services as well as some specific to the issues previously raised in this letter.

## Question 18: Should any of the proposed guidance be different for nonpublic entities (private companies and not-for-profit organizations)? If so, which requirement(s) and why?

As we have noted in comment letters on other topics, all NFPs are nonpublic entities. NFPs which are conduit debt obligors are considered public entities. This distinction is particularly relevant to colleges and universities, many of which issue tax-exempt debt. Despite the fact that these institutions have publicly traded debt, they have a different focus and a different set of financial statement readers and stakeholders than for-profit and publicly traded companies. While the ASU's proposed disclosure requirements may make sense for business and other public-interest entities that are moving toward the use of IFRS, requiring the same disclosures for all entities results in NFPs providing significant amounts of information, at a great cost to the organizations, that their financial statement users have not requested and may not find particularly valuable. This is particularly true of higher education institutions that conduct a significant amount of research under a hundreds, if not thousands, of contracts. The effort to these institutions of implementing accounting standards that were not drafted with them in mind creates a significant resource and financial burden, which can ultimately translate into an increased cost of education. We respectfully request that these factors, along with the inclusion of conduit debt obligors as public entities, be taken into consideration by the Board when determining the scope of proposed standards and that the Board scope the not-for-profit sector, including conduit debt obligors, out of the disclosure requirements of this proposal.

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In closing, we wish to express our appreciation for the opportunity to comment. We hope that the Board will address our concerns. We look forward to answering any questions the Board or the staff may have about our response. Please direct your questions to Sue Menditto at 202-861-2542 or <a href="mailto:sue.menditto@nacubo.org">sue.menditto@nacubo.org</a>.

Sincerely,

Susan M. Menditto

Director, Accounting Policy

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