

Exposure Draft ED/2010/6
Revenue from Contracts with Customers

response to exposure draft

22 October 2010

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We also champion high performance in public services, translating our experience and insight into clear advice and practical services. They include information and guidance, courses and conferences, property and asset management solutions, consultancy and interim people for a range of public sector clients.

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International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
Submitted electronically to www.ifrs.org

October 2010

Dear IASB secretariat

Exposure Draft ED/2010/6

Revenue from Contracts with Customers

CIPFA is pleased to present its comments on the proposals in this Exposure Draft, which have been reviewed by CIPFA's Accounting and Auditing Standards Panel.

The Exposure Draft follows up an earlier Discussion Paper 'Preliminary Views on Revenue Recognition in Contracts with Customers' to which CIPFA responded in July 2009. CIPFA considered that the proposals in the Discussion Paper were clearly and logically presented, and provided a useful basis for the development of an IFRS on Revenue Recognition, while noting that there were a number of significant issues which were not covered. In our view

- while the single revenue recognition principle based on control moved away from recognition based on risk and reward, risk and reward may need to be considered when determining where control lies in difficult cases.
- development was required to produce a decision-useful model which can practically be applied to long-term contracts which are difficult to characterise as transferring assets to the customer on a continuous basis

The Exposure Draft has made useful progress, and we strongly support the direction of travel. However, in our view further development is required in order to develop a model that can be applied consistently to all types of contracts, and which fully addresses issues relating to long-term contracts, including contracts for services. We accept that the satisfaction of performance obligations is a suitable basis for recognition of revenue, and that in many cases a performance obligation can be readily and objectively identified. However, further development on the 'control' concept is required, and it needs to be better explained.

Comments on specific questions for respondents are attached in an Annex.

I hope these comments are a helpful contribution to the development of an improved standard. If you have any questions about this response, please contact Steven Cain (e: steven.cain@cipfa.org.uk, t: +44(0)20 7543 5794).

Yours sincerely
Una Foy
Assistant Director
CIPFA
3 Robert Street, London WC2N 6RL

ANNEX

Responses to Questions for respondents

Q1: Paragraphs 12-19 propose a principle (price interdependence) to help an entity determine whether:

(a) to combine two or more contracts and account for them as a single contract;

(b) to segment a single contract and account for it as two or more contracts; and

(c) to account for a contract modification as a separate contract or as part of the original contract.

Do you agree with the principle? If not, what principle would you recommend, and why, for determining whether (a) to combine or segment contracts and (b) to account for a contract modification as a separate contract?

CIPFA agrees with the principle of interdependence as set out in the ED. Given that the assessment of revenue is at contract level, it is important that there is a mechanism for determining when contracts should be segregated or combined and how to treat modifications.

However, we are somewhat concerned that seven paragraphs are required to set out the principle. This is an area which could be helpfully clarified.

Q2: 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?

CIPFA agrees with this principle.

Q3: Do you think that the proposed guidance in paragraphs 25-31 and related application 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?

CIPFA is concerned that the guidance is not sufficiently well developed. Particularly in the context of a contract for the delivery of services rather than a physical asset, the concept of control may not be the most natural or intuitive, and may be difficult to apply.

Q4: The boards propose that if the amount of consideration is variable, an entity should recognise revenue from satisfying a performance obligation only if the transaction price can be reasonably estimated. Paragraph 38 proposes criteria that an entity should meet to be able to reasonably estimate the transaction price. Do you agree that an entity should recognise revenue on the basis of an estimated transaction price? If so, do you agree with the proposed criteria in paragraph 38? If not, what approach do you suggest for recognising revenue when the transaction price is variable and why?

CIPFA agrees that, where the amount of consideration is variable, revenue should be recognised where the transaction price can be reasonably estimated.

We note that the ED requires the transaction price to be calculated using the expected value approach proposed in the recent consultation on IAS 37 Provisions, contingent liabilities and contingent assets. In CIPFA's response to that consultation we expressed some reservations with this approach, which works best for for large populations of homogeneous items, and may be problematic in other cases.

Q11: The boards propose that an entity should disclose the amount of its remaining performance obligations and the expected timing of their satisfaction for contracts with an original duration expected to exceed one year. Do you agree with the proposed disclosure requirement? If not, what if any, information do you think an entity should disclose about its remaining performance obligations?

CIPFA agrees that the proposed disclosures would provide useful information.

However, application will be problematic for some entities with a large number of small contracts, especially as this forward looking information is unlikely to be contained within financial systems. It may be both difficult and costly to provide this information.

Q12: Do you agree that an entity should disaggregate revenue into the categories that best depict how the amount, timing and uncertainty of revenue and cash-flows are affected by economic factors? If not, why?

CIPFA agrees with this proposal, but we suggest that it would be beneficial if this disaggregation were more clearly aligned with the requirements of IFRS 8.

Q14: The proposed application guidance is intended to assist an entity in applying the principles in the proposed requirements. Do you think that the application guidance is sufficient to make the proposals operational? If not, what additional guidance do you suggest?

CIPFA considers that application guidance is extensive, but having regard to the diversity of arrangements (and the fact that the guidance is very compact compared to current US guidance) we consider that the level of guidance is about right. As noted in earlier answers, we consider that some clarification of the application of the control concept to e.g. service contracts is necessary, and this may also require changes to be made to the application guidance.