# EITF ABSTRACTS

**Issue No. 01-14**

**Title:** Income Statement Characterization of Reimbursements Received for "Out-of-Pocket" Expenses Incurred[1]

**Dates Discussed:** November 14–15, 2001; January 23–24, 2002

**References:** AICPA Statement of Position 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*
AICPA Audit and Accounting Guide, *Brokers and Dealers in Securities*

## ISSUE

1. Entities that provide services as part of their central ongoing operations generally incur incidental expenses that in practice are commonly referred to as "out-of-pocket" expenses. Those expenses often include, but are not limited to, expenses related to airfare, mileage, hotel stays, out-of-town meals, photocopies, and telecommunications and facsimile charges. In some cases, the service provider and the customer agree that the customer will reimburse the service provider for the actual amount of such expenses incurred. In other cases, the parties negotiate a single flat fee that is intended to compensate the service provider for both professional services rendered and out-of-pocket expenses incurred.

2. The scope of this Issue excludes transactions for which guidance is provided under categories (a) and (b) of the GAAP hierarchy, including:

- Sales of financial assets, including debt and equity securities, loans, and receivables
- Lending transactions

[1]At the January 23–24, 2002 EITF meeting, the Task Force agreed to recharacterize Topic No. D-103, "Income Statement Characterization of Reimbursements Received for 'Out-of-Pocket' Expenses Incurred," as an EITF Issue, rather than as an FASB staff announcement. No changes have been made to the guidance and no changes have been made to the effective date of this guidance. Accordingly, Topic D-103 has been renamed as Issue 01-14.

- Insurance and reinsurance premiums
- Transactions of broker-dealers that are within the scope of the AICPA Audit and Accounting Guide, *Brokers and Dealers in Securities*, and reimbursements received for expenses incurred in other specialized industries for which the accounting for such reimbursements is addressed in AICPA accounting and auditing guides.

3. The issue is whether reimbursements received for out-of-pocket expenses incurred should be characterized in the income statement as revenue or as a reduction of expenses incurred.

**EITF DISCUSSION**

4. The Task Force reached a consensus that reimbursements received for out-of-pocket expenses incurred should be characterized as revenue in the income statement. Issue No. 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent," and Issue No. 00-10, "Accounting for Shipping and Handling Fees and Costs," provide the principal support for the Task Force's consensus. In Issue 00-10, the Task Force reached a consensus that amounts billed for shipping and handling should be included in revenue. In reaching that consensus, the Task Force considered the fact that shipping and handling costs are sometimes billed at a zero margin. However, the Task Force concluded that the accounting for the transaction should not be affected by whether a company charges the customer separately for shipping and handling costs or includes the costs in the price of the merchandise. The Task Force agreed that, by analogy, the guidance in Issue 00-10 supports characterization of reimbursements received for out-of-pocket expenses incurred as revenue.

5. The guidance in Issue 99-19 indicates that whether a company should record revenue for the gross amount billed to a customer because it has earned revenue from the

sale of goods or services or the net amount retained (that is, the amount billed to the customer less the amount paid to a supplier) because it has earned a fee is a matter of judgment based on the relevant facts and circumstances. Issue 99-19 provides a series of indicators that should be considered in making that determination. The Task Force agreed that the following Issue 99-19 indicators support characterization of reimbursements received for out-of-pocket expenses incurred as revenue:

- Primary Obligor—the service provider (seller) is the primary obligor with respect to purchasing goods and services from third-party suppliers, such as airlines.
- Supplier Discretion—the service provider (seller) generally has discretion in selecting the supplier.
- Credit Risk—the service provider (seller) generally has credit risk because it typically receives reimbursement after the goods or services have been purchased.

6. The Task Force agreed that the following Issue 99-19 indicators support characterization of reimbursements received for out-of-pocket expenses incurred as a reduction of expenses incurred:

- Pricing—the service provider (seller) typically has no latitude in establishing the reimbursement price for the out-of-pocket expenses. Contractually, the service provider (seller) typically must invoice its customers for those expenses in an amount equal to the amount of the costs incurred.
- Zero Margin—the service provider (seller) earns no margin (that is, the price on the out-of-pocket expenses is fixed) because the arrangements generally state that those expenses are to be billed based on the actual cost incurred.

7. Based on the collective weight of the Issue 99-19 indicators (placing an emphasis on the primary obligor indicator) above, the Task Force agreed that characterization of reimbursements received for out-of-pocket expenses incurred as revenue is appropriate. The Task Force observed that that conclusion is consistent with the conclusion reached by analogy to Issue 00-10.

8. The Task Force agreed that income statement characterization as revenue of reimbursements received for out-of-pocket expenses incurred is also consistent with the guidance in SOP 81-1. Paragraph 15 of SOP 81-1 describes the types of contracts that are within the scope of that SOP, including time-and-material and cost-type contracts. Appendix B of SOP 81-1 describes variations of time-and-material contracts, including contracts in which materials are billed at cost, and cost-type contracts that require reimbursement of costs incurred in addition to a fixed fee. SOP 81-1 suggests that those arrangements are simply different methods of pricing and that the amounts billed in each case should be characterized as revenue. Paragraph 55 of SOP 81-1 states that "the estimated revenue from a contract is the total amount that the contractor expects to realize from the contract." Although there may be instances in which the contractor acts solely as an agent, paragraph 59 of SOP 81-1 states that in cases in which the contractor acts as a principal "the contractor should include in revenue all reimbursable costs for which he has risk or on which his fee was based at the time of bid or negotiation."

9. The consensus in this Issue should be applied in financial reporting periods beginning after December 15, 2001. Upon application of the consensus in this Issue, comparative financial statements for prior periods should be reclassified to comply with the guidance in this Issue. If it is impracticable to reclassify prior-period financial statements, disclosure should be made of both the reasons why reclassification was not made and the effect of the income statement characterization guidance in this Issue on the current period. Early adoption of the provisions of this Issue is permitted.

**STATUS**

10. No further EITF discussion is planned.