ICGN
International Corporate Governance Network

Attn: Technical Director
Financial Accounting Standards Board
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Submit via email: director@fasb.org

12 March 2012

Dear Technical Director

Re: File Reference No. 2011-230, FASB/IASB Exposure Draft, Proposed Accounting Standards Update (Revision of Exposure Draft Issued June 24, 2010), Revenue Recognition (Topic 605), Revenue from Contracts with Customers.

We are writing on behalf of the International Corporate Governance Network ("ICGN")

The ICGN is a global membership organization of institutional and private investors, companies, and advisors from 50 countries. Our investor members are responsible for global assets under management of $18 trillion USD.

The ICGN's mission is to raise standards of corporate governance worldwide. The ICGN encourages cross-border dialogue at conferences and influences corporate governance public policy through ICGN Committees. We promote best practice guidance, encourage leadership development and keep our members informed on emerging issues in corporate governance through publications and the ICGN website. To compliment this, the ICGN is also developing a comprehensive ESG training program for investment professionals which is being launched in March 2012. For more information about the ICGN, its members and activities please visit our website: www.icgn.org.

The purpose of the Accounting and Auditing Practices Committee ("A&A Practices Committee") is to address and comment on accounting and auditing practices from an international investor and shareowner perspective. The Committee, through collective comment and engagement, strives to ensure the quality and integrity of financial reporting around the world. http://www.icgn.org/accounting-and-auditing-practices-committee.php

Thank you for providing us with the opportunity to comment on the FASB/IASB Proposed Accounting Standards Update (Revised), Revenue Recognition (Topic 605), Revenue from Contracts with Customers. Revenue recognition is generally viewed as the most important line item in the financial statements. We are pleased that individuals and organizations are being invited to comment on whether the proposals are clear and can be applied in a way that effectively communicates to users of financial statements the economic substance of an entity's contracts with customers and that the FASB/IASB are jointly considering comment letters.

In general, the ICGN agrees that the core principle of the proposed standard is that an entity should recognize revenue from contracts with customers when it transfers goods or services to the customer in the amount of consideration the entity receives, or expects to receive, from the customer. Moreover, the ICGN supports the FASB/IASB goal to create a single revenue recognition standard to improve both IFRSs and U.S. GAAP by:

- Removing inconsistencies in existing requirements;
- Providing a more robust framework for addressing revenue recognition issues;
- Improving comparability across companies, industries and capital markets;
- Requiring enhanced disclosure; and
- Clarifying accounting for contract costs.

More specifically, our answers to the six questions posed are as follows:

Question 1: *Paragraphs 35 and 36 specify when an entity transfers control of a good or service over time and, hence, when an entity satisfies a performance obligation and recognises revenue over time. Do you agree with that proposal? If not, what alternative do you recommend for determining when a good or service is transferred over time and why?*

ICGN supports the criteria for transfer of control specified in paragraphs 35 and 36. We believe paragraph 35(b) will be the clause applied in most cases. The criteria in 35(b) (i) and (iii) seem reasonably clear. 35(b) (ii) may need some clarification; what is meant by "work in process presently controlled by the entity"? We would also recommend adjusting 35 (b) (ii) by adding so it would read '…the entity fulfilling the remainder of the contract would not have the benefit of any asset presently controlled by the entity, *related to the work of the entity it is contractually supposed to complete.*' This separates benefits from assets that are not related to the initial contract from benefits to which the re-performing entity might be entitled.

In reference to 35(b) (iii) some may find the distinction between having "a right to payment" and, for instance, being "virtually certain to receive payment" fairly arbitrary, and whilst in general we support requiring a right to payment which is a more objective condition (as long as the right can reasonably be expected to be exercised by the entity and fulfilled by the counterparty, i.e. if the right has economic substance) we have concerns that an entity may still be able to manage earnings .

Question 2*: Paragraphs 68 and 69 state that an entity would apply IFRS 9 (or IAS 39, if the entity has not yet adopted IFRS 9) or ASC Topic 310 to account for amounts of promised consideration that the entity assesses to be uncollectible because of a customer's credit risk. The corresponding amounts in profit or loss would be presented as a separate line item adjacent to the revenue line item. Do you agree with those proposals? If not, what alternative do you recommend to account for the effects of a customer's credit risk and why?*

As stated in our earlier submission, a customer's credit risk should not be reflected in revenue. Credit provisions should be reported on a separate line in the income statement as otherwise this reduces the comparability of revenues. Presenting any difference between revenue and value of receivable as a line item adjacent to the revenue line item is a good solution.

Question 3: *Paragraph 81 states that if the amount of consideration to which an entity will be entitled is variable, the cumulative amount of revenue the entity recognises to date should not exceed the amount to which the entity is reasonably assured to be entitled. An entity is reasonably assured to be entitled to the amount allocated to satisfied performance obligations only if the entity has experience with similar performance obligations and that experience is predictive of the amount of consideration to which the entity will be entitled. Paragraph 82 lists indicators of when an entity's experience may not be predictive of the amount of consideration to which the entity will be entitled in exchange for satisfying those performance obligations. Do you agree with the proposed constraint on the amount of revenue that an entity would recognise for satisfied performance obligations? If not, what alternative constraint do you recommend and why?*

ICGN agrees that the fact that consideration must be estimated should not preclude recognition of revenue. The conditions in paragraphs 82 are necessary, but more guidance is needed in this area. In particular, the concept of "reasonable assurance" is in need of further clarification as otherwise an entity could manage its earnings. This qualitative standard is used repeatedly in the exposure draft.. For example, it is not clear to us from the definition of reasonable assurance why a performance based asset management fee based on annual returns may not be recognized quarterly if the return is measured reliably (see IE 13) as it meets the criteria under paragraph 81(a) and (b).

However, we do agree with the proposed constraint on the amount of cumulative revenue be limited to the amount of the transaction price to which the entity is reasonably assured to be entitled.

Question 4: *For a performance obligation that an entity satisfies over time and expects at contract inception to satisfy over a period of time greater than one year, paragraph 86 states that the entity should recognise a liability and a corresponding expense if the performance obligation is onerous. Do you agree with the proposed scope of the onerous test? If not, what alternative scope do you recommend and why?*

ICGN supports recognition of liability/expense for onerous performance obligations. We do not support the scope restriction. Recognition of liability/expense should be required for all performance obligations subject to materiality - not only for those which the entity expects to satisfy over a period of time greater than 1 year since inception of the contract (paragraphs 35 and 36 do not give this time restriction)

Question 5: *The boards propose to amend IAS 34 and ASC Topic 270 to specify the disclosures about revenue and contracts with customers that an entity should include in its interim financial reports. The disclosures that would be required (if material) are:*

- *The disaggregation of revenue (paragraphs 114 and 115)*
- *A tabular reconciliation of the movements in the aggregate balance of contract assets and contract liabilities for the current reporting period (paragraph 117)*
- *An analysis of the entity's remaining performance obligations (paragraphs 119–121)*
- *Information on onerous performance obligations and a tabular reconciliation of the movements in the corresponding onerous liability for the current reporting period (paragraphs 122 and 123)*
- *A tabular reconciliation of the movements of the assets recognized from the costs to obtain or fulfil a contract with a customer (paragraph 128).*

Do you agree that an entity should be required to provide each of those disclosures in its interim financial reports? In your response, please comment on whether those proposed disclosures achieve an appropriate balance between the benefits to users of having that information and the costs to entities to prepare and audit that information. If you think that the proposed disclosures do not appropriately balance those benefits and costs, please identify the disclosures that an entity should be required to include in its interim financial reports.

ICGN agrees that disclosures should meet user needs. This principles based approach to disclosure is appreciated. Reporting entities should be sensitive to user needs and listen to user requests. This should be explicitly stated in the standard or the basis for conclusions. The ICGN also emphasizes that users require comparable disclosure to understand the amount, timing and uncertainty of revenue and cash flows, and that harmonization of disclosures in IFRS with US GAAP is important.

ICGN agrees that disaggregated information about revenues is useful. An entity should be able to classify its contracts both by service type, maturity and geographically in a similar way to segmental information. It would be useful for investors to see more than one cut of the business if it is in different geographies and lines of business. The classification, albeit aggregated into portfolios with different characteristics, should reconcile with the consolidated statement of income.

A tabular reconciliation of the movements in the aggregate balance of contract assets and contract liabilities for the current reporting period is necessary to provide insight into these accounts and the effects on quarterly earnings. An analysis of the entity's remaining performance obligations is also helpful to users. We take note of the fact that qualitative information may be sufficient to satisfy this requirement. We also support the requirement to provide information on onerous performance obligations and a tabular reconciliation of the movements in the corresponding onerous liability for the current reporting period as well as a tabular reconciliation of the movements of the assets recognized from the costs to obtain or fulfil a contract with a customer.

The ICGN represents users of information and will naturally focus on the benefits of disclosure. However, as far as we can see the information required to be disclosed will be readily available in entities' information systems. Hence the costs to provide the information should not be prohibitive.

Question 6: *For the transfer of a non-financial asset that is not an output of an entity's ordinary activities (for example, property, plant and equipment within the scope of IAS 16 or IAS 40, or ASC Topic 360), the boards propose amending other standards to require that an entity apply (a) the proposed requirements on control to determine when to derecognise the asset, and (b) the proposed measurement requirements to determine the amount of gain or loss to recognise upon derecognition of the asset. Do you agree that an entity should apply the proposed control and measurement requirements to account for the transfer of non-financial assets that are not an output of an entity's ordinary activities? If not, what alternative do you recommend and why?*

ICGN finds that the proposals to amend IAS 16, IAS 38 and IAS 40 (and corresponding US standards) flows logically from proposals to replace IAS 11 and IAS 18. However, we would like to add that the revenue recognition project has demonstrated that the concept of control must be supported by guidance and clarification to be operative for more complex businesses.

We continue to believe that “control” as a criterion in financial reporting may prove problematic in some areas.. If the goods are still in the physical possession of the seller, are incomplete and continuing to undergo production, such that they cannot be employed by the customer, we do not believe that the seller is entitled to recognize revenue even if the contract states otherwise. We support the conditions of severability and usability in the definition of transfer in order to use control as a criterion for revenue recognition.

If you would like to discuss any of these points, please do not hesitate to contact ICGN Executive Director, Carl Rosen, at +44 207 612 7084 or by e-mail at carl.rosen@icgn.org.

Thank you for your consideration.

Yours sincerely,

Christianna Wood
Chairman of the ICGN Board of Governors

Janine Guillot
Co-Chair, ICGN Accounting and Auditing Practices Committee

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