Naarden, December 10, 2007

To: PAAin E Revenue Recognition Working Group,

Dear Sirs,

It is my pleasure to herewith submit my comments to your paper on Revenue Recognition.

I firmly believe that standards for financial reporting cannot be set without having a coherent conceptual framework for financial reporting. In my opinion IASB has started is standard setting process without having this framework ready and that is why some standards, like IAS 18 and 11, appear not to be consistent. Unfortunately, it looks like your working group fell into this trap as well.

I have therefore not addressed your specific questions, but instead tried to answer the question of revenue recognition from a line of reasoning about financial reporting. I realize that this reasoning is far from complete, but in my opinion such reasoning is the only starting point for setting standards.

My ideas on the subject are included in the attachment to this letter. I appreciate having the opportunity to provide you with my views.

Sincerely,

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1. Aspects of a framework for financial reporting.

A framework is a set of assumptions, concepts, values and practices that constitutes a way of viewing reality (source: American Heritage Dictionary). The purpose of the framework for financial reporting is to provide that set for financial reporting. The set of assumptions, concepts, values and practices are the basis for principles. A principle is a fundamental source of something (source: Oxford English Dictionary), i.e. a financial reporting principle is a description of a fundamental requirement that financial reports should meet in order to achieve the desired way of viewing reality. Elaboration of the principles for the purpose of applying these to the various aspects of financial reporting is done in standards. Standards do not constitute new principles, but only give a description of the application of the principle.

Principles are a basis for viewing reality. Inherently principles will fall short of being able to provide thru their application a perfect view of reality. Financial reports are no more than a model of the real world and as such their usefulness in reflecting reality is different for different aspects of that reality. In the development of standards this inherent shortcoming of a model should constantly be recognized and accepted.

The conceptual framework of the IASB is as yet not completed, from which one might conclude that the desired way of viewing reality is not established yet, at least the coherence of the principles and related standards is not visible. In other words, current IFRS may have been written without guidance from a full and complete concept. It is far from certain that, once this concept is available, all current IFRS fit in and fall neatly into their place. One cannot but hope that once it is available that the current set of IFRS only needs little adaptation. Disastrous it would be if the framework is written in a way to compulsory, artificially, unnaturally include all existing IFRS.

2. Introduction to a framework for financial reporting.

The purpose of financial reporting has its origin in the function of an entity, which is in essence to convert resources into products for exchange in a market. The purpose of financial reporting follows as being reporting (obviously in financial or, monetary terms) on, i.e. providing a view of, the result of the conversion and exchange process realized by the entity. Reporting is done by those to whom the resources and the conversion and exchange process are entrusted to (= management). Users of financial reports are those who have provided resources. Different resource providers will have different levels of interest in the financial report. Those providers whose reward is fully dependant on the result of the conversion and exchange process (=investors) have the highest interest. Others have less interest in the result to the extent that they have provided resources at conditions (=creditors), which make their reward less dependant on that outcome. Risks and rewards are (considered) key factors in the resource allocation decisions of investors and creditors and these factors should be the drivers for the principles and standards for financial reporting.

The result of the conversion and exchange process presents all differences, none excluded, between the value of the resources provided at the beginning of the conversion and the exchange process and the value of resources returned to investors at the end of it. The result is inclusive of all increases and decreases of value, because all value changes have one thing in common: all value changes are a result of management's decisions.

If the conversion and exchange process is continuous (=continuity assumption) and if a financial report covers only a certain time period of that continuing process, than the use of the report is extended beyond merely reporting on the result. Firstly, users are interested in the value and the composition of the result in order to assess whether management has realized the result that was required for the period reported on. Secondly, users are interested in both the composition of the present result and in the capacity of the residual resources to generate future results in order to be able to identify and assess risk factors with respect to those future results. The need to provide a breakdown of the result in (among other) revenue recognized originates from these (assumed) information needs of resource providers.

Result is defined as income minus expense, whereby revenue is just one of the various types of income. Income (or loss) is a realizable, i.e. a probable and measurable, change in value of the assets and liabilities of an entity. Assets are resources from which measurable future benefits are probable to flow to the entity.

The unique aspect of an asset is that, its realization, i.e. initiating the flow of the benefits embodied in the assets to the entity, is at the sole discretion of management. Once management's decision to realize the benefit has been taken is it probable that the flow will indeed reach the entity and becomes a (new) asset itself.

Revenue is the type of income that arises from the exchange process the entity is engaged in, i.e. the exchange in a market of one asset for another asset. The key aspect of this description of revenue is asset. The definition of an asset contains a number of requirements that all need to be met before a resource can be considered an asset. These requirements are (1) measurable, (2) future benefits, (3) probable and (4) to flow to the entity. The answer to the question when and to what amount revenue is to be recognized is simply when the resource acquired in the exchange meets the requirements for being recognized as an asset.

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