Fixing Social Security

Eric Rothenburg's article in April ("Social Security: A Macroeconomic Issue") was an excellent summary of the situation. It proposed solutions in accordance with the problem of demographics, something that privatization does not do.

I would like to suggest another idea. Through the years, the role of human beings in production has been partially replaced by machines. Why not place a Social Security tax on those machines, or some variation of it that would recognize the full import of the production process? Best of all, the machines would never collect. ❑

Theodore Gruber, CPA
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The author responds:

I enjoyed the humor and sarcasm in Gruber's response to my article; however, at the time of writing, it appears that the idea of privatizing a portion of Social Security withholdings is waning in the House and the Senate. If we look at the 2005 volatility of the equity markets, we notice that oil spikes, lackluster corporate earnings, and an increase in interest rates have caused a deterioration in many equity valuations.

On a personal note, I rolled over an IRA-CD account into three separate equity mutual funds in January 2000. Examining my statements for the last quarter, I am still averaging unrealized losses of 50% to 60%. While I realize that those rollovers occurred at the peak of the Dow and Nasdaq, I certainly would not want to have relied on these accounts for retirement. Let us keep Social Security intact for lower- and middle-income taxpayers—the people who really need it. ❑

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Revenue Recognition for Software

The April article "Revenue Recognition for Software Products with Multiple Deliverables" states that: "Companies such as Microsoft and Computer Associates have recognized revenue from license fees when the software was shipped to the customer. The amount and timing of revenue recognition is complicated, however, by multiple-element arrangements that provide for multiple software deliverables."

My understanding is that at least until 2002, Computer Associates used a provision in the AICPA's SOP 97-2 that allowed for the residual method of revenue recognition. Under that method, the contract terms determine that amount of revenue recognized, whereas the remainder remains unearned. This method is referenced in the footnotes of Computer Associates' 2001 financial statements.

Thus, for Computer Associates the shipping of software does not trigger recognition of revenue. In fact, this method has subsequently been questioned by the SEC because of claims of "earnings management," even though it was more conservative in nature. ❑

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The authors respond:

The reader is correct in that Computer Associates used the residual method to account for revenue recognition on sales of software. We did not intend to imply that Computer Associates recognized all of the revenue in a multiple-element arrangement at the time the software was shipped. Under the residual method, however, revenue is recognized (assuming all revenue recognition criteria are met) for the delivered elements when the software is shipped.

For example, consider a company that sells a software product for $95,000. The license arrangement always includes one year of "free" postcontract customer support (PCS). The annual renewal price of PCS is $15,000. Thus there is vendor-specific objective evidence (VSOE) for the PCS—the undelivered element. Because the software is never sold separately (it always includes one year of PCS), there is no VSOE for the delivered element.

If all revenue recognition criteria are met on the delivered elements (i.e., persuasive evidence of an arrangement exists, delivery has occurred, the vendor's fee is fixed or determinable, and collectability is probable), then using the residual method would result in a deferral of $15,000—the VSOE for the undelivered element. The remaining $80,000 is assigned to the delivered element and is recognized upon shipment. ❑

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