Tech Center

Panel Leaves Untouched Rule Letting Firms Book Revenue From Bartered Ads

By Elizabeth MacDonald
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In a move expected to cheer Web advertisers, U.S. accounting rule makers left virtually untouched a standard that lets companies book revenue from advertising barter transactions, a popular practice with Internet businesses.

But the rule making panel at the Financial Accounting Standards Board inserted a big wrinkle intended to end an accounting abuse in which cash-strapped Internet companies "gross up," or increase, the revenue they earn from these deals, an abuse the Securities and Exchange Commission wanted stopped.

A growing number of dot-com companies now routinely swap advertising with other Web sites, in which they advertise each other's companies on their Web sites. To book these advertising barter transactions, the e-businesses then typically record offsetting revenue and expense amounts for these exchanges.

Given that Internet companies are now routinely valued on their revenues -- since most of them generate losses -- regulators have grown worried that some companies have overstated the revenue received in these deals, in order to pump up their stocks.

One Big Caveat

Specifically, the accounting rule makers said companies can continue to book revenue they receive from bartered advertising, with one big caveat. The FASB panel, the emerging issues task force, says companies can only include revenue from advertising barter transactions so long as they have a history of receiving cash for "similar advertising transactions," and those deals didn't take place more than six months prior to when the barter actually occurred, says Tim Lucas, a research director at the FASB.

"That could stop the practice of grossing up revenue, since companies will now have to shell out cash in order for these revenue amounts to pass muster," says Robert Willens, a managing director at Lehman Brothers Inc. And if the abuse was curbed, says Henry Blodget, a senior Internet analyst at Merrill Lynch & Co., it "would certainly change the valuations for some companies considerably."

SEC Chief Accountant Lynn Turner applauded the changes, noting that they "should certainly enhance the information that investors are going to be receiving on these advertising barter transactions."

The FASB now wants the barter amounts disclosed in a footnote, something companies now don't routinely do.
Barter Transactions

For instance, VerticalNet Inc., a Horsham, Pa., operator of online business-to-business trading communities, said barter transactions "accounted for approximately 21% of total revenues" in its 1999 third quarter. SportsLine USA Inc., a sports-related Internet site, said barter transactions came to about 18% of total revenue for the third quarter of 1999.

James Marks, an e-commerce analyst at Credit Suisse First Boston, says his research so far shows about a dozen publicly traded Internet companies had booked revenue for these deals, with some amounts reaching 20% of the total.

While Mr. Lucas says the changes could affect most media companies, some analysts say many don't have to worry. For example, CBS Corp. last year agreed to furnish Medscape Inc., a New York health Web site company, with $150 million in promotional services, including plugs on its TV and radio stations, in exchange for a 35% stake in the new company. "We have 14 of these kinds of promotion for equity swap arrangements," says Dana McClintock, a CBS spokesman.

Mr. Willens says "television networks like CBS who do these transactions likely won't run into any problems with the accounting changes because they have a history of selling advertising for cash, plus the equity stakes they get are easily valued." He adds though that it won't be smooth sailing for Internet companies, "given that they have a spotty history of receiving cash in these deals, due to the newness of the industry."

Lise Buyer, an Internet analyst at Credit Suisse First Boston in Palo Alto, Calif., says "the specter of these changes" has caused many companies to not include these barter transactions in revenue at all. "Companies are now erring on the side of caution," she says.

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