



Sir David Tweedie Chairman of the International Accounting Standards Board 30 Cannon Street

London EX4M 6XH United Kingdom

Phone Fax E-mail Date

+49.89.35757-1556 +49.89.35757-1555 crispin.teufel@linde.com October 21, 2010

Re: IASB Exposure Draft ED/2010/6
Revenue from Contracts with Customers

Comment Letter of The Linde Group

Dear Sir David,

The Linde Group is a world leading gases and engineering company with almost 48,000 employees working in more than 100 countries worldwide. In the 2009 financial year it achieved sales of EUR 11.2 billion. We offer a wide range of compressed and liquefied gases as well as chemicals and we are therefore an important and reliable partner for a huge variety of industries. Our engineering division is successful throughout the world, with its focus on promising market segments such as olefin plants, natural gas plants and air separation plants, as well as hydrogen and synthesis gas plants.

The Linde Group is listed in the leading German share index (DAX) and prepares its consolidated financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. In 2009, revenues from our engineering division amounted to EUR 2.3 billion. Revenue recognition for long term construction contracts is hence very important for the financial statements and the financial performance of The Linde Group. We therefore appreciate the opportunity to comment on the Exposure Draft Revenue from Contracts with Customers from an engineering industry perspective.

We acknowledge the boards' intention to eliminate inconsistencies in the current standards and create a principle-based and easy-to-apply revenue recognition model with a wide-spread applicability.



Despite our general support, we have some concerns with the proposals in the ED. These are in detail set out in the appendix to this letter.

Our main concern relates to the boards' attempt to develop a single model for revenue recognition. As laid out in our answers to the questions raised by the boards, the proposed model does not reflect economic realities, especially relating to construction contracts. In our opinion, long term customer-specific construction contracts would need a different basis of accounting. The unit of account should be the managed contract as it reflects the management's view and therefore is the relevant level of information meeting investors' information needs. We would therefore recommend leaving long-term customer-specific construction contracts scoped out of IAS 18 and not trying to artificially deal with all possible contracts in just one model.

The Linde Group being a German stock-listed company has for long time accounted for construction contracts applying the completed-contract method in compliance with German Commercial Code. We have gone through extensive and extremely cost-intensive projects in order to implement IFRS and especially the requirements of IAS 11 *Construction Contracts* and therefore feel very competent to state that the implementation of the percentage of completion method has significantly increased the decision usefulness of financial information provided to users and that the implementation of this standard bridged successfully the gap between the way we steer our business and the investors' information needs.

The current regulation for such contracts in IAS 11 *Construction Contracts*, which requires the application of percentage-of-completion (PoC) accounting is well established and understood since many years and industrial companies throughout the world successfully adopted these requirements. The treatment proposed in the exposure draft could lead to completed contract accounting for many of these contracts and performance obligations. We believe that this would result in disturbed earnings figures and therefore raise the need for giving additional information based on the current revenue recognition model for their analysts. Therefore, the regulations proposed in the exposure draft would mean a step-back instead of a step ahead for us.

In our opinion the revenue figure in the financial statements would depict an entity's performance more faithfully if it represented the activities carried out by the entity to fulfil a contract with a customer and not be based on the transfer of control over a promised good or service.

The proposed requirements would neither reflect the way the customer views the contracted project nor be consistent with the entity's internal management steering the business on the level of contracts rather than single performance obligations. Even if required by IFRSs, a contract that is managed as one will not be split into several performance obligations for internal controlling purposes as this will only artificially split the contracts for external reporting purposes without providing additional information value from the managements perspective. As a result, the proposal will lead to a drifting apart of internal and external accounting. We do not understand why the IASB is currently shifting away from its reliance on management's view of an entity's business instead of further clarifying the principles of this approach.

Furthermore, the huge implementation costs for many entities will in most cases outweigh the decision-usefulness of the information provided. We would therefore recommend the boards to significantly reduce the implementation effort for many entities by adopting a final guidance that leads to the result that the accounting



for construction contracts does not significantly differ from the existing well established standards on revenue recognition.

If you have any questions or remarks, please do not hesitate to contact us. We would be happy to discuss any of our comments with you at your convenience.

Yours sincerely,

Björn Schneider Head of Group Accounting & Reporting Crispin Teufel Head of IFRS Competence Center & External Reporting



# Appendix: answers to the questions raised in the ED

## Question 1:

Paragraphs 12-19 propose a principle (price interdependence) to help an entity determine whether:

- a) to combine two or more contracts and account from them as a single contract;
- b) to segment a single contract an account for it as two or more contracts; and
- c) to account for a contract modification as a separate contract or as part of the original contract. Do you agree with that principle? If not, what principle would you recommend, and why, for determining whether (a) to combine or segment contracts and (b) to account for contract modifications as a separate contract?

We agree with the proposed principles for combining and segmenting contracts. In our opinion, a clear cut definition of the contract to which the following revenue recognition steps shall be applied is the first important step for creating useful information. We also agree that price interdependences would help an entity determine whether to combine or segment contracts.

However, regarding contract modifications, we do not agree with the proposed separation criteria. In our opinion, once a contract is defined, subsequent modifications should generally be accounted for as part of the original contract. This would reflect the way such modifications are managed internally, as variations and change orders are subject to the original contract conditions. They will affect the original contract's timetable and will have to be dealt with by the original contract management.

In our view, relying solely on price interdependencies will require a degree of management judgement and subjectivity that might impair the decision usefulness of information given. It would furthermore burden management to document its considerations on price interdependencies for each single contract modification. This would not only cause a significant workload, it could also cause disturbances in earning recordings and thereby reduce the decision usefulness of financial statement information.

We are convinced that only in those very rare circumstances, where a modification is functionally different and managed independently from the existing contract, a separate revenue recognition scheme might lead to more useful information than a combined one.

Should the boards decide to retain its proposal, we would like to point out the importance of the word "indicators" in paragraph 13. In the construction business, contract modifications frequently occur long after the original contract is entered into but have nevertheless highly interdependent prices. This interdependence would need to be negated, if the indicator "near or at the same time" would be changed to a criterion.



### Ouestion 2:

The boards propose that an entity should identify the performance obligations to be accounted for separately on the basis of whether the promised good or service is distinct. Paragraph 23 proposes a principle for determining when a good or service is distinct. Do you agree with that principle? If not, what principle would you specify for identifying separate performance obligations and why?

We generally agree with the boards' proposed principle that an entity should identify the performance obligations to be accounted for separately on the basis of whether the promised goods or services are distinct or not. However, for several reasons explained below, we do not agree with the principle set out in paragraph 23 for determining when a good or service is distinct.

As a general principle in paragraph 20, an entity shall evaluate the term of the contract and its customary business practices for determining whether to account for each promised good or service as a separate performance obligation. When defining the meaning of a distinct good or service, paragraph 23(a) contains the criterion "the entity, or another entity, sells an identical or similar good or service separately". Especially with regards to highly specialized customer businesses, we strongly object to the reference of another entity's business practices as we consider it more meaningful – as stated in the general principle - to refer to the entity's own business practice. Financial statements are intended to present the entity's performance not other entities' hypothetical performance.

Regarding the definition of a "distinct function", the proposal requires a good or service to have "utility either on its own or together with other goods or services". Firstly, we would expect further guidance to make this requirement more operational. Furthermore, we consider this criterion difficult with regard to construction contracts. A construction may contain several project steps but those are usually all strongly interwoven. That is why those contracts are negotiated and managed together and should be treated as one single performance obligation rather than segregated into parts. This would a) reflect the way the customer in most cases looks at the contracted project and b) be consistent with the entity's management way of steering the business, namely on the level of contracts rather than single performance obligations.

Treating the described construction contract as one project would also solve the problem that the proposal is lacking guidance on how an entity should account for a distinct bundle of goods and services, if the goods and services in the bundle have different patterns of performance.

Furthermore, we would propose deleting the requirement of a distinct profit margin as we regard the requirement as misleading and not useful in practice. We acknowledge that the boards added the requirement of a distinct profit margin since they were concerned that requiring an entity to estimate a selling price for a good or service might result in information that would not be useful to users of financial statement. Requiring a



distinct profit margin does in our opinion not solve this problem as the selling price is very often not related to a certain margin but to external circumstances as e.g. market situation or negotiation skills.

We therefore propose to require separation only if an entity is – with reliable evidence – able to determine the price at which it would sell the specific good or service separately. This requirement would be more useful and also preclude artificially splitting customer-specific construction contracts. Those usually treat with goods and services with non-distinct functionality in the sense above and are never comparable to one another in terms of pricing and thus evidence of stand-alone selling prices of such goods or services might be scarce and their determination would require a high level of judgement and would not lead to reliable and useful information.

## Question 3:

Do you think that the proposed guidance in paragraphs 25-31 and related application guidance are sufficient for determining when control of a promised good or service has been transferred to a customer? If not, why? What additional guidance would you propose and why?

We acknowledge the boards' decision that revenue recognition should only be possible if a contract with a customer exists. Taking this as a starting point and following the general principle that on entering a contract with a customer, an entity obtains rights to receive consideration from the customer and assumes obligations to transfer goods or services to the customer (performance obligations), we agree that revenue recognition has to be based on the fulfilment of the obligation. We take note of the boards' decision to apply a control based rather than an activity based revenue recognition principle as control based revenue recognition relies on external factors whereas activity based revenue recognition relies on internal factors which are considered by the boards to be judgemental and open to misuse.

However, we regard the control based approach as unacceptable. In case of delivery of goods, transfer of control might be a good indicator for revenue recognition, but we do not believe that the principle of control is able to be the all-comprehensive principle for revenue recognition.

We have significant concerns regarding the indicators of control provided in paragraph 30 of the ED. Defining control as an entity's ability to direct the use of, and receive the benefit from, a good or service is not clearly translated in these four indicators. We agree that "legal title" and "physical possession" are indicators for the above definition, whereas the indicators "customer specific" and "unconditional obligation to pay" are rather an indicator for a transfer of risks and rewards but are not directly linked to the transfer of control.

This inconsistency together with the proposal's unweighted enumeration of the four indicators will lead to different interpretations within sometimes similar industries and thereby impair the comparability of financial statements between different companies.



Furthermore, the proposed control concept together with the four criteria would require completed contract accounting for certain long term contracts where PoC accounting was applied under the principles stipulated in IAS 11 *Construction Contracts*. The boards regard PoC accounting as applicable under their proposal if one interprets the business activity taking place as a continuous transfer of control that takes place with progress of work performed. Whether a continuous transfer of control occurs or not requires a lot of judgment and therefore won't be applied consistently between different entities. This would further diminish comparability of financial statements and thereby reduce their decision usefulness.

As a result, leaving the proposal as it is could force many companies to change their business model surrounding the structure of their contracts. Entities could opt for sequences of short term contracts rather than long term contracts to recognise revenue progressively, rather than only at the end of a contract. It might also be that entities formerly entering into turn key lump sum on their construction contracts would change to several separate contracts to mitigate the effect of revenue recognition at the end of the contract term. We question whether accounting should potentially change business practice in this regard.

The current approach under IAS 11 was well established over many years and provided useful information to users – especially external analysts. It also ensures cohesiveness between internal and external accounting in revenue recognition for customer specific long term construction contracts. We are therefore asking the general question why the consistent and established risk and rewards approach shall be replaced by an impracticable and inconsistent control based approach lacking clear guidance that might in practice lead to less decision-useful information.

# Question 4:

The boards propose that if the amount of consideration is variable, an entity should recognise revenue from satisfying a performance obligation only if the transaction price can be reasonably estimated. Paragraph 38 proposes criteria that an entity should meet to be able to reasonable estimate the transaction price.

Do you agree that an entity should recognise revenue on the basis of an estimated transaction price? If so, do you agree with the proposed criteria in paragraph 38? If not, what approach do you suggest for recognising revenue when the transaction price is variable and why?

We do not agree that an entity should recognise revenue on the basis of an estimated transaction price. The scenario in example 19 and other possible scenarios reveal the subjectivity of such estimations. The high degree of management judgment would reduce the decision usefulness of financial statement information.



### Ouestion 5:

Paragraph 43 proposes that the transaction price should reflect the customer's credit risk if its effects on the transaction price can be reasonably estimated. Do you agree that the customer's credit risk should affect how much revenue an entity recognises when it satisfies a performance obligation rather than whether the entity recognises revenue? If not, why?

We agree that considering customer's credit risk in the amount of recognised revenue will lead to a more accurate recognition of revenue in certain circumstances, but we do not believe that it will always correctly reflect economic reality.

Reducing the amount of promised consideration to reflect the customer's credit risk only makes sense under the general assumption that credit spreads comparable to those in e.g. loan agreements were included in the agreed transaction price. However, this assumption is not valid; in an industrial company's reality, unlike financial institutions, the agreed consideration will in most cases not include a surcharge for the customer's credit risk as this will simply be unenforceable in contract negotiations.

Furthermore, especially in industrial companies where financial risk measurement is not a core business and thus sophisticated measurement systems are not in place, the assessment of customer's credit risk is a process requiring a lot of management judgement. This judgment would endanger the reliability of information provided. As a result, the reflection of customer credit risk in revenue would not lead to comparable and therefore decision-useful financial statements.

In paragraph B78 and B79 of the proposed application guidance, the boards restrict the credit risk consideration to those contracts in which the effect of the customer's credit risk on the transaction price is material. We would propose to include this materiality statement into the standard and to provide further guidance for this materiality judgment. Furthermore we would restrict the consideration of customer's credit risk to those cases where it is recognised in the pricing.

We are moreover convinced that subsequent changes in the credit risk estimate should be reflected in revenue rather than other income to be cohesive with the cash flow statement.



### Ouestion 6:

Paragraphs 44 and 45 propose that en entity should adjust the amount of promised consideration to reflect the time value of money if the contract includes a material financing component (whether explicit or implicit). Do you agree? If not, why?

We generally agree with the principle to reflect the time value of money if the contract includes a material financing component (whether explicit or implicit). We also acknowledged the example in the exposure draft on how to account for the time value of money for payments in arrears and in advance.

### Question 7:

Paragraph 50 proposes that an entity should allocate the transaction price to all separate performance obligations in a contract in proportion to the stand-alone selling price (estimated if necessary) of the good or service underlying each of those performance obligations. Do you agree? If not, when and why would that approach not be appropriate, and how should the transaction price be allocated in such cases?

We generally agree that an entity should allocate the transaction price to all separate performance obligations in a contract in proportion to the stand-alone selling price (estimated if necessary) of the good or service underlying each of those performance obligations.

Nevertheless, we want to point out that determining stand alone selling prices for goods or services will most probably be subject to a high degree of uncertainty with net selling prices being in many cases not observable or only existing in bandwidths. The determination of such bandwidths of net sales prices is extremely burdensome and subjective so that reliability of information might be impaired.

A prerequisite for a sound allocation of revenue amongst different goods or services is the correct identification of separate performance obligations. We refer to our answers to question two regarding the challenges within the model proposed by the boards.

Long term contracts in our business are generally negotiated between the contractor and customer as a single transaction with a single profit margin. A contract may contain several phases, some being – if priced separately – more profitable than others. Some phases might even be unprofitable, even when the contract as a whole is profitable. When it is deemed necessary to break such a contract into segments for the purpose of recognizing revenue, allocating the transaction price to the different performance obligations in proportion to their stand-alone selling price this would result in big disturbances in recognition of revenues or even losses. In



our opinion, this would not fulfil the boards' intention to report useful information about the amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

## Question 8:

Paragraph 57 proposes that if costs incurred in fulfilling a contract do not give rise to an asset eligible for recognition in accordance with other standards (for example, IAS 2 or ASC Topic 330; IAS 16 or ASC Topic 360; and IAS 38 Intangible Assets or ASC Topic 985 on software), an entity should recognise an asset only if those costs meet specific criteria.

Do you think that the proposed requirements on accounting for the costs of fulfilling a contract are operational and sufficient? If not, why?

We generally agree with the proposal for capitalization of contract costs that relate primarily to activities to fulfil the contract but do not transfer goods or services to the customer. Nevertheless, for making the application more operational we would ask for further guidance regarding costs qualifying for recognition.

This refers especially to overhead costs. The ED permits in paragraph 58 "allocations of costs that relate directly to the contract activities" and mentions costs of contract management in this context. This wording does not clearly state if overhead cost that can be allocated in general qualify for capitalization. Under the existing IAS 11 their capitalization is required. Is it really the boards intention to restrict capitalization of such cost, if yes, what are the reasons for this?

# Question 9:

Paragraph 58 proposes the costs that relate directly to a contract for the purpose of

- (a) recognising an asset for resources that the entity would use to satisfy performance obligations in a contract and
- (b) any additional liability recognised for an onerous performance obligation.

Do you agree with the costs specified? If not, what costs would you include or exclude and why.

We generally agree with the costs specified in paragraph 58 for the purpose of a) recognising an asset for resources that the entity would use to satisfy performance obligations in a contract and b) any additional liability recognised for an onerous performance obligation.



However, we would like to point out a perceived contradiction between the measurement of an onerous performance obligation and the measurement of obligations fulfilled by undertaking a service according to the current proposal in *ED/2010/1 Measurement of Liabilities in IAS 37*. Whereas onerous performance obligations are measured at the costs the entity expects to incur to fulfil its contractual obligations, ED/2010/1 requires including a profit margin into the measurement of obligations fulfilled by undertaking a service. In our opinion, this is contradiction as the outflow of resources is not different just because the liability is based on an onerous performance obligation or an obligation fulfilled by undertaking a service.

Furthermore, we see a potential inconsistency with the framework: The recognition of a provision for onerous contracts on performance obligation level is only in compliance with the framework if the unit of account upon which to decide if a liability exists or not is the performance obligation level. We do not believe that this is the right level to report on management performance, since a) the revenue allocation required by the standard does not represent the way management calculates its contract prices, b) an entity's management steers their business on the level of contracts or sometimes key accounts rather than on the level of performance obligations and hence c) also external users of financial information consider the contract level as the most relevant level to assess management's performance. The information regarding onerous performance obligations is therefore not relevant for users of financial statements and hence not decision useful.

## Question 10:

The objective of the boards' proposed disclosure requirements is the help users of financial statements understand the amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. Do you think the proposed disclosure requirements will meet that objective? If not, why?

The question is not if disclosure requirements will meet the objective to help users understand the amount, timing and uncertainty of revenue and cash flows. The question is whether the required information will influence decision making. We share the boards' view that it should be the objective to provide readers of the financial statements with relevant information that enables them to make their assessment of timing and amount of future revenue and cash flows. Anyhow, we doubt that the information required by the boards meets this objective since we believe that narratives within the notes are hardly taken into account by users.

We are furthermore convinced that the most important information – namely the information about recurring and non-recurring revenue – should be addressed on the level of the statement of comprehensive income rather than in the notes. This is primarily a matter of revenue segmentation and the correct reflection of the underlying business model. Narratives should in this context be used as a corrective of misunderstandings rather than as a pro-active instrument for principal, essential information.

Furthermore, the proposed guidance is not definitive enough and leaves too much room for interpretations for the entities leading to non-comparable information. The additional disclosure requirements will thereby burden

1820-100 Comment Letter No. 328



Page 12

entities with significant additional costs without improving the decision-usefulness of financial statement information.

It seems also worth mentioning that some of the required disclosures in the exposure draft are also required via the operating segment information under IFRS 8 and should therefore not be doubled in the financial statements.

## Question 11:

The boards propose that an entity should disclose the amount of its remaining performance obligations and the expected timing of their satisfaction for contracts with an original duration expected to exceed one year.

Do you agree with that proposed disclosure requirement? If not, what, if any, information do you think an entity should disclose about its remaining performance obligations?

In our opinion the requirement for an entity to disclose its remaining performance obligations and the expected timing of their satisfaction for contracts with an original duration expected to exceed one year is excessive and due to the uncertainty especially in the construction industry and the related high amount of judgement does not lead to decision useful information. We would rather include figures like order intake or orders on hand as these are less subjective and should be available for internal management objectives in nearly all industrial companies.

We also do not support including a reconciliation of contract balances as proposed in paragraph 73(b) and 75 as we do not consider that this disclosure provides useful information.

# Question 12:

Do you agree that an entity should disaggregate revenue into the categories that best depict how the amount, timing and uncertainty of revenue and cash flows are affected by economic factors? If not, why?

We agree that entities should determine the categories that best depict how the amount, timing and uncertainty of revenue and cash flows are affected by economic factors as this will not be uniform. In our opinion the disagreggation of revenue on the operating segments provides the best decision useful information to the users of the financial statements.





### Question 13:

Do you agree that an entity should apply the proposed requirements retrospectively (i.e. as if the entity had always applied the proposed requirements to all contracts in existence during any reporting periods presented)? If not, why?

Is there an alternative transition method that would preserve trend information about revenue but at a lower cost? If so, please explain the alternative and why you think it is better.

As a construction company Linde has a large number of outstanding long term construction contracts. Applying the proposed requirements retrospectively would result in very high effort and hence very high costs for The Linde Group. These costs do not only arise for training, operating and maintaining two revenue recognition systems and assuring both systems can be reconciled into each other when there are contract amendments or other adjustments. They already arise for the first transition as each of our highly individualized contracts would have to be assessed separately. We are therefore questioning if the effort does not outweigh the expected increase in decision usefulness.

Retrospective application will be onerous to many entities but a prospective application might cause the same problems. Applying the requirements in IAS 11 on existing long-term construction contracts and the proposed model on new contracts would also require entities to keep up two accounting systems for the sometimes long contract duration of existing contracts.

For consistency with the other changes that are currently proposed by boards, we would nevertheless recommend a retrospective application in accordance with the other proposed changes, i.e. at the earliest with an applicable date in 2014. Hereby, it is very important to keep in mind that a guidance which does not require significant changes compared to the existing IAS 18 and IAS 11 would strongly ease the implementation effort and impact for many entities, after all in the construction industry.



### Ouestion 14:

The proposed application guidance is intended to assist an entity in applying the principles in the proposed requirements. Do you think that the application guidance is sufficient to make the proposals operational? If not, what additional guidance do you suggest?

In general, we appreciate the proposed application guidance as it in fact assists an entity in applying the principles in the proposed requirements. Nevertheless, as already mentioned above, we would rather prefer clear cut principles in the standard that would not require additional clarifications in the application guidance. The application guidance should rather concentrate in providing examples for an operational application of the standard. Alternatively should the boards keep pace with their proposed model, more accounting guideline should be provided to ensure a consistent application of the proposed model.

# Question 15:

The board proposes that an entity should distinguish between the following types of product warranties:

- a) a warranty that provides a customer with coverage for latent defects in the product. This does not give rise to a performance obligation but requires an evaluation of whether the entity has satisfied its performance obligation to transfer the product specified in the contract.
- b) a warranty that provides a customer with coverage for faults that arise after the product is transferred to the customer. This gives rise to a performance obligation in addition to the performance obligation to transfer the product specified in the contract.

Do you agree with the proposed distinction between the types of product warranties? Do you agree with the proposed accounting for each type of product warranty? If not, how do you think an entity should account for product warranties and why?

We acknowledge the boards' intention to separate warranties if they contain a separate performance obligation, but we consider the proposed split between warranties for latent defects and warranties for faults that arise after delivery inappropriate.

We would rather propose to split warranties with regards to the underlying business model and economic reality of an entity. If it is part of an entity's core business to offer extended warranties to its customers, these extensions are in fact distinct and therefore are separate performance obligations. This would justify a deferral of revenue.



Nevertheless, most entities regard warranties as required additions that are closely interrelated with the overall contract and are not distinct performance obligations. In such cases, the performance obligation is satisfied and revenue can be recognized when the customer obtains control of the product, i.e. the product is transferred to the customer. Revenue should therefore be fully realized at this time. Withholding revenue is no solution as it would not show an entity's economic reality. Any obligations to cover latent defects can then be included as provisions.

We therefore see no convincing reason for the proposed split. In our opinion, faults that were not obvious at the time of transfer as well as faults that arise within the warranty period but after the product was transferred both cause a present obligation with uncertainty about future outflows of economic benefits and should therefore be accounted for as provisions under IAS 37. In fact, as ED/2010/1 regarding the measurement of liabilities in IAS 37 proposes to include a margin into the measurement of performance obligations that the entity plans to fulfil by itself. The obligation amount would therefore be the same, no matter if measured as deferred revenue or provision. Presenting the obligation as a provision would in our opinion (a) better take into account the uncertainty of the future outflow of resources for the addressee of the financial statements and (b) better reflect the nature of the obligation as integral part of the primary performance obligation, namely the delivery of goods or rendering of services.

Furthermore, in practice it will often be impossible from a legal point of view to differentiate and follow up in accounting, if a product return belongs to one or another category of warranty. This occurs after all for warranties without legal or contractual obligation that are fulfilled as a gesture of goodwill. They are currently treated as constructive obligations in accordance with IAS 37. It is unclear how entities should account for them in the proposed model.

## Question 16:

The boards propose the following if a licence is not considered to be a sale of intellectual property:

- a) if an entity grants a customer an exclusive licence to use its intellectual property, it has a performance obligation to permit the use of its intellectual property and it satisfies that obligation over the term of the licences; and
- b) if an entity grants a customer a non-exclusive licence to use its intellectual property, it has a performance obligation to transfer the licence and it satisfies that obligation when the customer is able to use and benefit from the licence.

Do you agree that the pattern of revenue recognition should depend on whether the licence is exclusive? Do you agree with the patterns of revenue recognition proposed by the boards? Why or why not?



We do not understand the distinction made between exclusive and non-exclusive licenses. We understand the boards' intention to distinguish between exclusive licenses which are correlated with the seller's outstanding obligation not to violate the exclusivity clause and non-exclusive licenses where such obligation does not exist.

Nevertheless, we do not believe that the obligation to refrain from further use of the exclusive license hinders the transition of "control" about the transferred license – especially not from a customer's perspective. Control over the license is transferred when the customer obtains the right to use the underlying intellectual property as he wants irrespective if the right of use represents the whole substance of the licensed intellectual property or not. This is also the concept of ED/2010/9, where the partial disposal of an asset in the form of an unconditional right of use might lead to the recognition of day-one gains or losses.

In this context we furthermore do not understand why intangible assets are explicitly scoped out from ED/2010/9 and despite of this fact explicitly referred to in ED/2010/6 paragraph B32. We feel that there is urgent need for alignment between the two exposure drafts – on the level of detail regulations as well as on the level of the basic underlying concepts.

## Question 17:

The boards propose that in accounting for the gain of loss on the sale of some non-financial assets (for example, intangible assets and property, plant and equipment), an entity should apply the recognition and measurement principles of the proposed revenue model. Do you agree? If not, why?

We agree that the proposed principles should be applied in accounting for gains and losses on the sale of some none-financial assets.