

13 March 2012

International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH
United Kingdom

By email to: commentletters@ifrs.org

IASB ED/2011/6 – Revenue from Contracts with Customers

Dear Sirs

I am writing on behalf of AFME (the Association for Financial Markets in Europe) to respond to IASB ED/2011/6 – Revenue from Contracts with Customers (the “ED”). AFME is, as you know, the leading European trade association for firms active in investment banking and securities trading; it was established in 2009 as a result of the merger of LIBA (the London Investment Banking Association) and the European Branch of SIFMA (the US-based Securities Industry and Financial Markets Association), and thus represents the shared interests of a wide range of participants in the wholesale financial markets.

General Comments

As financial institutions, the activities of AFME members are to a large extent excluded from the scope of this ED, their main activities being principally covered by the accounting standards on financial instruments. The impact of the proposals for AFME members is thus largely restricted to the treatment of certain fees, and to transactions relating to certain non-financial items such as commodities. Our comments therefore pertain to these areas only.

The ED has not, in our view, adequately explained the reasons for introducing an entirely control-based model for revenue recognition: we believe this represents a substantial shift in approach from the current derecognition model for non-financial assets under both IFRS and US GAAP (which combine control with risks and rewards).

In addition to the above, we do not believe the guidance in Paragraphs B38-48 on recognising revenue for transactions that incorporate some form of repurchase agreement is clear or consistent. This is in part because restrictions on recognising revenue due to the retention of options or other similar rights is more usually a product of a risk and rewards model, and hence is difficult to link to a pure control-based model.

Association for Financial Markets in Europe

We note in particular that:

- The examples appear to assess future control (e.g. the ability to access the asset in the future) as being more important than current control.
- Under a control-based model, a forward or call option only restricts a transferee if the asset is not readily obtainable regardless of the price.
- The examples allow the consideration of time value of money, but do not allow consideration of other potentially relevant factors such as forward price curves, etc.
- The examples do not contemplate situations where the repurchase price is variable, such that the arrangement may fall either under case (a) of case (b) of Paragraph B40.
- Paragraph B43 requires consideration of the customer's economic incentive to exercise an option; this is inconsistent with Paragraph B40, and also appears to be in substance a risk and rewards analysis.
- The model appears to be a purely quantitative analysis of what constitutes a financing arrangement and does not allow the use of qualitative factors or judgment.

Our responses to the questions on pages 14-16 of the ED are set out below.

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?

Although we agree with the principle of recognising revenue over time when an entity satisfies a performance obligation over time, we do not (as noted above) in general support a purely control-based model as the basis for revenue recognition. Consequently, we do not support the proposals in Paragraphs 35 and 36 for identifying when a good or service is transferred over time.

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?

We agree with this proposal. Promised consideration is a receivable, and hence a financial asset. In our view, impairment of this asset is more appropriately assessed under IFRS 9/IAS 39 or ASC Topic 310, and should accordingly be treated separately from the revenue item.

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?

We support the inclusion of a constraint on recognition of variable revenue. However, we are unsure as to the appropriateness of the term “reasonably assured”: this appears to introduce yet another subjective threshold into accounting literature, which we believe is unnecessary and will create further confusion. Notwithstanding this, we do not believe that this will change current practice in our industry significantly.

We also have concerns over the indicators of “predictive” experience detailed in Paragraph 82 for determining whether the “reasonably assured” threshold has been met for variable revenue. We believe a better approach would be for the entity to arrive at a measurement of the amount of variable consideration to which the entity is entitled consistent with the ED principle that requires entities to recognise the expected value or most likely amount of expected revenue. In other words being susceptible to measurement factors outside the entity's control does not imply a lack of “entitlement” to that revenue. We note as well that the factors listed should be described as factors that may be predictive rather than factors that will always be predictive as this will vary.

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?

We do not agree with the scope of the onerous test for a number of reasons. In particular:

- Some of our members think the time restriction is somewhat arbitrary. A contract of less than one year may be onerous and an entity should be able to account for it as such. Moreover, contracts of less than one year's duration may span different accounting periods and hence, in their view, the recognition of expenses and liabilities for such contracts may still be significant. Other members believe the distinction the Board has drawn between contracts of more than one year and those of less than one year is appropriate provided the test is applied at the overall contract level (see point below), as it represents a pragmatic approach that strikes an appropriate balance between cost and benefit.
- Some members also believe the most appropriate approach is to apply the onerous test at the contract level. They do not think it should be applied at the performance obligation level within a contract as this could result in recognition of a liability for one performance obligation within a contract which, when taken overall, is not onerous.

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 (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 recognised 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.

While supporting the overall objectives of the disclosure requirements, we believe that the required disclosures are overly detailed and formulaic, rather than allowing preparers to exercise their judgment in the manner described in Paragraph 110. We also find the proposed disclosures to be overly focused on the mechanics of accounting rather than on providing users with useful and relevant information, and that the time, effort and cost of implementing and maintaining the necessary reporting systems for preparers would greatly outweigh any potential benefits to the users of financial statements.

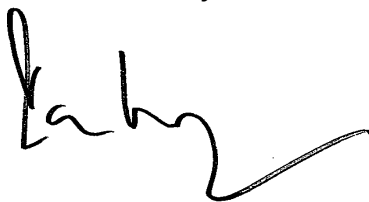
Notwithstanding our comments above, we believe the Boards should address interim reporting as part of a separate project rather than extending interim reporting requirements on an ad-hoc, and potentially inconsistent, basis through the development of other standards.

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?

We agree that an entity should apply consistent principles to account for the transfer of non-financial assets regardless of whether or not they are an output of its ordinary activities. However, as noted in our comments above, we have significant reservations as to whether the control based requirements proposed in the ED provide an appropriate basis for accounting for such transfers.

I hope the above comments are helpful. We would of course, as always, be pleased to discuss any points which you may find unclear, or where you believe AFME members might be able to assist in other ways.

Yours faithfully



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