

Submitted electronically via IASB website

Sir David Tweedie
Chairman
International Accounting Standards Board
1st Floor 30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Espoo June 18, 2009

Re: Nokia's comments on 'DISCUSSION PAPER Preliminary Views on Revenue Recognition on Contracts with Customers' December 2008

Dear Sir,

We are pleased to submit our comments for your consideration regarding the discussion paper 'Preliminary Views on Revenue Recognition on Contracts with Customers' issued by the IASB and FASB in December 2008.

We welcome the efforts of the boards in developing the discussion paper and we support the boards' objective to adopt a single revenue recognition principle and standard. We agree that the existing revenue recognition guidance is lacking in terms of consistency, simplicity and clarity.

While we appreciate that many of the proposals put forward by the boards represent improvements over existing guidance, we would like to highlight our concerns as follows:

- It is our opinion that revenue recognition based on the transfer of goods and services to the customer will not provide decision-useful information to users of financial statements in all cases. Instead, as set out in our response to question 9, we propose an alternative revenue recognition model based on the completion of revenue-generating activities.
- We raise concerns regarding the heightened potential for abuse in revenue recognition if return rights are treated as performance obligations.
- We are uncertain whether all sales incentives give rise to a performance obligation. Further, we question whether the incremental benefit to users from this change will exceed the expected increase in related costs of compliance. We welcome detailed implementation guidance that would provide clarity on the boards' views on the treatment of sales incentives.
- We ask for clarification related to the boards' proposal on estimated stand-alone selling prices with specific reference to post-contract customer support not sold separately by the entity or its competitors.

If you have any questions in relation to this letter please do not hesitate to contact me at Nokia.

Yours faithfully,

Anja Korhonen
Senior Vice president, Corporate Controller
Nokia Corporation

Question 1

Do you agree with the boards' proposal to base a single revenue recognition principle on changes in an entity's contract asset or contract liability? Why or why not? If not, how would you address the inconsistency in existing standards that arises from having different revenue recognition principles?

Nokia Response

We support the boards' objective to adopt a single revenue recognition principle. We agree that a single revenue recognition principle would improve the usefulness of information provided in financial statements both in terms of consistency of application to specific transactions and the comparability of application across companies. Further, a single robust revenue recognition principle strongly linked to the underlying concepts set out in the *Framework for the Preparation and Presentation of Financial Statements* will provide needed clarity to preparers and users of financial statements.

A contract is the underlying mechanism by which commercial enterprises engage in business and generate revenue. Therefore, we feel that it is logical to link revenue recognition to the rights obtained and obligations assumed in the underlying contract with the customer whether written, unwritten, explicit or implicit.

However, as discussed in our response to question 9 below, we support an alternative revenue recognition trigger than as proposed in the discussion paper.

Question 2

Are there any types of contracts for which the boards' proposed principle would not provide decision-useful information? Please provide examples and explain why. What alternative principle do you think is more useful in those examples?

Nokia Response

We do not think that the proposed principle will provide decision-useful information for construction-type contracts in which the asset under construction is not transferred to the customer on a continuous basis. As discussed in our response to question 9 below, we support an alternative revenue recognition trigger than as proposed in the discussion paper.

Question 3

Do you agree with the boards' definition of a contract? Why or why not? Please provide examples of jurisdictions or circumstances in which it would be difficult to apply that definition.

Nokia Response

We agree with the boards' definition of a contract and do not anticipate significant difficulties in applying this definition to Nokia's transactions.

Question 4

Do you think the boards' proposed definition of a performance obligation would help entities to identify consistently the deliverables in (or components of) a contract? Why or why not? If not, please provide

examples of circumstances in which applying the proposed definition would inappropriately identify or omit deliverables in (or components of) the contract.

Nokia Response

We agree with the boards' definition of a performance obligation and do not anticipate significant difficulties in applying this definition to identify contract deliverables.

Question 5

Do you agree that an entity should separate the performance obligations in a contract on the basis of when the entity transfers the promised assets to the customer? Why or why not? If not, what principle would you specify for separating performance obligations?

Nokia Response

We believe that the main objective for identifying separate performance obligations in a given contract is to represent faithfully the pattern by which the entity's financial position is enhanced through its ordinary activities. As discussed in our response to question 9 below, we support an alternative revenue recognition trigger than as proposed in the discussion paper.

Question 6

Do you think that an entity's obligation to accept a returned good and refund the customer's consideration is a performance obligation? Why or why not?

Nokia Response

We agree that a return right granted to a customer is a performance obligation arising from the original contract with the customer. In effect, the entity receives payment from the customer in exchange for two promises made to the customer: one promise to deliver a good and a second promise to allow the customer to put the sold goods back to the entity over a specified time period with an exercise price equal to the original value of the underlying goods and the value of the return right.

Although we agree in principle with the discussion paper's view on return rights, we hope that the boards could provide implementation guidance that would clarify the measurement of the return rights and the bookkeeping for return rights:

- Our view is that the measurement model for the return rights should emphasise simplicity as the adoption of a complex option-pricing model is not likely to produce significant benefits to users. We feel that an expected cost plus margin model would likely suffice and would correspond to the actual pricing of return rights by entities.
- Regarding the bookkeeping, our interpretation of the discussion paper is that the return right is to be treated as a service provided to the customer. As such, the revenue related to the return right would be recognized irrespective of the outcome (i.e. return or no return) as the services are provided over the return period. It would then follow that any refunds paid to the customer as a result of returns would be treated as a cost of the return right rather than as a deduction from revenue.
 - Although we believe that the recognition of refunds as a cost may be justifiable from a theoretical standpoint, we are concerned that this practice could create opportunities for entities to inflate reported revenue. Thus, we are interested to understand what measures will be put in place (if any) to deter abuse in this area.

Question 7

Do you think that sales incentives (eg discounts on future sales, customer loyalty points and 'free' goods and services) give rise to performance obligations if they are provided in a contract with a customer? Why or why not?

Nokia Response

We agree that, in many cases, sales incentives granted to a customer comprise performance obligations arising from the original contract with the customer. Similar to the case of return rights, the entity provides the customer with one promise to deliver a good and an option which the customer may exercise to execute a future transaction.

We urge the boards to provide implementation guidance on this topic that would provide clarity on the measurement and bookkeeping for the many different types of sales incentives. For example, would there be any instances where the boards feel that the cost of sales incentives would be booked as a reduction of revenue?

Further, we question whether all the different types of sales incentives have been properly evaluated against the framework proposed in the discussion paper as we are uncertain whether all sales incentives could be classified as performance obligations. Given that the incremental administrative cost needed to track each sales incentive as a performance obligation may be significant, we feel that this issue needs to be considered carefully with the incremental benefits to users clearly identified.

Take the example of a sale of goods on credit with a cash payment discount. The pricing of the contract incorporates both the value of the goods and the implicit financing cost (reflecting customer credit risk, time value, etc). The cash payment discount is set equal to the implicit financing cost. Taken from this perspective, it is clear that the economic substance of a cash payment discount is similar to that of the return right except that the cash payment option allows the customer to reverse the financing component of the transaction instead of the sale of goods component.

Given this similarity, should the treatment of the cash payment correspond to that of the return right? Or, in contrast to the return right, does the exercise of the cash payment option represent a failed sale since the 'customer financing sale' remains undelivered at the date of exercise?

Question 8

Do you agree that an entity transfers an asset to a customer (and satisfies a performance obligation) when the customer controls the promised good or when the customer receives the promised service? Why or why not? If not, please suggest an alternative for determining when a promised good or service is transferred.

Nokia Response

We agree that the transfer of an asset to a customer occurs when control of the promised good or service has passed to the customer. We believe that the transfer of control approach generally results in more representationally faithful outcomes than the risks and rewards of ownership approach. Further, the concept of control is aligned with the definition of an asset found in the *Framework for the Preparation and Presentation of Financial Statements*.

However, we do not agree that the transfer of an asset to a customer should necessarily trigger the recognition of revenue by an entity. As discussed in our response to question 9 below, we support an alternative revenue recognition trigger than as proposed in the discussion paper. In addition, a potential implication of the revenue recognition model proposed in the discussion paper is a shift in focus towards

the distinction between the delivery of goods and services. We question whether this may result in inconsistent application in practice with an emphasis on contractual / legal form over economic substance.

Question 9

The boards propose that an entity should recognise revenue only when a performance obligation is satisfied. Are there contracts for which that proposal would not provide decision-useful information? If so, please provide examples.

Nokia Response

Nokia's proposal for an improved revenue recognition model

We do not believe that the revenue recognition proposal as laid out in the discussion paper will always provide decision-useful information for users of financial statements. In particular, we believe that the proposed revenue recognition principle would not be appropriate for long-term construction-type contracts where the value of inventory assets is enhanced by activities performed by the entity. Instead, we feel that revenue recognition that reflects the revenue generating activities of the entity would provide a more faithful representation of the underlying economic transactions/events and enable users to discern the implications of these transactions/events on future performance. We have identified two key revenue generating activities that we believe convey decision-useful information to users:

1. Entering into a contract with a customer to provide goods or services.
 - a. We feel that contracts should play a prominent role in revenue recognition as they provide price discovery¹ for an entity's goods and services. Prior to the agreement of a contract, the entity does not have sufficiently reliable evidence to place a value on its goods and services.
2. Fulfillment of contractual performance obligations to provide goods or services.
 - a. We also emphasise the efforts expended by the entity to fulfill its contractual performance obligations as they are an essential element of an entity's ordinary activities and are directly attributable to the generation of revenue.

We contend that it is the combination of the two revenue generating activities that enhance the value of an entity's asset and provide the basis for the recognition of revenue. Therefore, both activities would need to be in place prior to the recognition of revenue by an entity. As a practical guideline, in transactions where the period between contract signing and delivery of contractual goods is short, an exemption could be available allowing entities to recognize revenue upon delivery given that revenue recognition according to delivery will not result in a materially different pattern of revenue recognition than our model would propose.

For example, an entity with finished goods inventory could only recognize the revenue related to those goods when a contract with a customer for the sale of those goods has been agreed². Similarly, an entity without any inventory on hand that has agreed a contract with a customer for the sale of a good could only recognize revenue related to that sale as it progresses towards the fulfillment of its performance obligation to provide the good. Again, in practice, revenue recognition according to delivery will only result in a materially different pattern of revenue for long-term contracts (i.e. where the period between contract signing and delivery is long).

¹ Contracts provide price discovery for an entity's goods and services in a similar way that the interaction of buyers and sellers on an active liquid stock exchange provide price discovery for a publicly-held stock.

² Note that the entity may not be able to justify recognition of the full contractual consideration as revenue at the contract agreement date to the extent of unsatisfied performance obligations related to the distribution and transport of the goods to the customer.

Justification for Nokia's proposed revenue recognition model

Consistent with the *Framework for the Preparation and Presentation of Financial Statements*, we feel that a primary objective of financial statements is to facilitate users' evaluation of the stewardship of management and provide users with a basis for predicting future financial position and financial performance. In other words, financial statements should reflect the impact of significant past events and transactions as well as enable users to understand their implications on future performance. With these objectives in mind, we feel that an activity-based revenue recognition model such as the one described above would provide more decision-useful information to users of financial statements than the model proposed in the discussion paper.

For example, users would be interested to know that an entity has signed a significant contract for a sale of goods with an important customer. The signing of the contract conveys both confirming value of management's efforts to win the contract as well as predictive value related to the future benefits to arise from the contract. However, under existing standards, the contract would not be reflected in the entity's financial statements even if the entity already has the contracted quantity of goods in its finished goods inventory and delivery costs are expected to be minimal (i.e. the expected cost of remaining performance is minimal).

Similarly, users would be interested in evaluating the activities of the entity. However, under the proposal in the discussion paper, an entity ('entity A') at a zero stage of completion in a long-term contract would present similar financial performance in its profit and loss statement as an entity ('entity B') in a similar long-term contract but at an 80% stage of completion despite the fact that entity B is clearly in an advantageous position to entity A. Thus, it would appear that the financial performance presented in entity B's profit and loss statement would not faithfully represent its actual performance under the terms of the contract.

Further, contrast the accounting treatment for an entity ('entity C') that holds finished goods inventory with a book value of 25 to an entity ('entity D') that owns an actively-traded stock with a market value of 25. The following day, entity C signs a contract with a fixed price for the sale of the finished goods for 40 and the market price of entity D's stock rises to 40. Although the underlying financial position of both entities is equal on day 2, only entity D would recognize the improvement in its financial position on day 2 in its profit and loss statement. In accordance with Concepts Statement No.5, both the inventory held by entity C and the stock held by entity D are 'salable at reliably determinable prices without significant effort' on day 2.

Question 10

In the boards' proposed model, performance obligations are measured initially at the original transaction price. Subsequently, the measurement of a performance obligation is updated only if it is deemed onerous.

- a) Do you agree that performance obligations should be measured initially at the transaction price? Why or why not?

Nokia Response

For the reasons presented in the discussion paper (pattern of revenue recognition, complexity, risk of error), we agree that performance obligations should be measured initially at the transaction price.

- b) Do you agree that a performance obligation should be deemed onerous and remeasured to the entity's expected cost of satisfying the performance obligation if that cost exceeds the carrying amount of the performance obligation? Why or why not?

Nokia Response

We agree that onerous performance obligations should be remeasured to the expected cost of satisfying the performance obligation. The recognition of onerous performance obligations provides timely, decision-useful information to users of financial statements regarding the occurrence of significant adverse changes in an entity's circumstances. Further, recognition of an onerous obligation is consistent with the criteria for recognition of elements of financial statements as set out in the *Framework for the Preparation and Presentation of Financial Statements*.

- c) Do you think that there are some performance obligations for which the proposed measurement approach would not provide decision-useful information at each financial statement date? Why or why not? If so, what characteristic of the obligations makes that approach unsuitable? Please provide examples.

Nokia Response

We do not foresee any issues with the application of proposed measurement approach.

- d) Do you think that some performance obligations in a revenue recognition standard should be subject to another measurement approach? Why or why not? If so, please provide examples and describe the measurement approach you would use.

Nokia Response

We believe that all performance obligations that fall under the scope of the revenue recognition standard should be subject to a common measurement approach.

Question 11

The boards propose that an entity should allocate the transaction price at contract inception to the performance obligations. Therefore, any amounts that an entity charges customers to recover any costs of obtaining the contract (eg selling costs) are included in the initial measurement of the performance obligations. The boards propose that an entity should recognise those costs as expenses, unless they qualify for recognition as an asset in accordance with other standards.

- a) Do you agree that any amounts an entity charges a customer to recover the costs of obtaining the contract should be included in the initial measurement of an entity's performance obligations? Why or why not?

Nokia Response

We agree that costs are recognized as expenses when incurred unless eligible for capitalization in accordance with other standards.

We understand that the discussion paper was not intended to address the accounting for costs associated with contracts with customers. Still, we are very interested to understand whether it is appropriate to interpret the boards' stance regarding capitalization of costs and the persistent emphasis on an 'assets and liabilities' approach throughout the discussion paper as a signal that

application of the matching concept will be significantly reduced if not eliminated altogether. We understand that, in most cases, the assets and liabilities approach should produce similar outcomes as the matching principle approach. However, we would welcome implementation guidance illustrating the application of the assets and liabilities approach.

- b) In what cases would recognising contract origination costs as expenses as they are incurred not provide decision-useful information about an entity's financial position and financial performance? Please provide examples and explain why.

Nokia Response

We do not foresee any cases where the capitalization of contract origination costs would provide decision-useful information. In our opinion, capitalized contract origination costs do not meet the definition of an asset as set out in the *Framework for the Preparation and Presentation of Financial Statements*.

Question 12

Do you agree that the transaction price should be allocated to the performance obligations on the basis of the entity's stand-alone selling prices of the goods or services underlying those performance obligations? Why or why not? If not, on what basis would you allocate the transaction price?

Nokia Response

We agree that the most objective, reliable and intuitive allocation method is based on the stand-alone selling prices of the goods or services.

Question 13

Do you agree that if an entity does not sell a good or service separately, it should estimate the stand-alone selling price of that good or service for purposes of allocating the transaction price?

Nokia Response

When an entity does not sell a good or service separately, we agree that that stand-alone selling price should be estimated for purposes of allocating the transaction price. As pointed out in the discussion paper, limitation of the use of estimates can create patterns of revenue recognition that do not faithfully represent the economic position and performance of entities in a contract. Specifically, limitations on the use of estimates may result in overstatement in the value of an entity's performance obligations.

Furthermore, limitation of the use of estimates may exacerbate inconsistencies in the remeasurement of performance obligations (i.e. deferred revenue) in current practice. Current practice in the valuation industry is to apply an exit price (i.e. expected cost plus margin) valuation methodology when determining the fair value of deferred revenue balances assumed by an acquirer in a business combination whereas the deferred revenue balances were originally recognized by the acquiree using a transaction price methodology under a restriction on the use of estimates.

For example, consider an entity that sells a software license to a customer for 50 EUR that entitles the customer to unspecified content and software upgrades and enhancements for a year. The unspecified upgrades and enhancements are not sold on a standalone basis but their value is estimated at 5 EUR. Under existing practice, the entity may recognize deferred revenue of 50 EUR. However, if the same entity were acquired in a business combination on the following day, the same deferred revenue balance might be written down to EUR 5 as a purchase accounting adjustment.

NOKIA

9 (9)

Specifically with respect to the estimation of standalone selling prices, we would like to see implementation guidance illustrating the measurement of post-contract customer support (PCS) in cases where PCS is not sold separately by either the entity or competitors.