



International Accounting Standards Board  
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## **Exposure Draft (ED) of Revenue from Contracts with Customers**

Dear Sirs

We very much welcome the opportunity to comment on the above-captioned exposure draft.

### **General comments**

In Holcim's view, the driving factor for preparing standards on financial reporting should be information usefulness. Holcim is concerned that the ED has been issued without a thorough conceptual debate on why revenue is an important figure, what it should represent and why it provides useful information.

The ED proposes that revenue should be recognised only when control of goods and services is transferred to the customer. Holcim does not support that model and considers that the IASB has not explained why the proposals would result in more useful information.

Holcim believes that financial statements would be most decision-useful were revenue to be considered a measure of activity carried out to fulfil a contract with a customer, subject to specific conditions being met. The aforementioned objective is currently met under IAS 18 *Revenue* by recognizing revenue only when the significant risks and rewards of ownership of the goods have been transferred to a customer and under IAS 11 *Construction Contracts* by applying the percentage of completion method.

In the Basis for Conclusions to the ED, the IASB infers that the proposed model will bring discipline to the earnings process approach. While Holcim might agree that the proposals have such potential, this improvement does not justify in itself the fundamental change made to the revenue recognition model. A change in the revenue recognition model may prove costly to preparers of financial statements; as such, Holcim believes that these costs should be justified. Therefore, we believe that a proper assessment should be carried out to conclude whether the benefits of a new standard on revenue recognition would outweigh its costs.

Putting aside Holcim's fundamental concern regarding the model for revenue recognition and focusing on the model proposed, our response can be summarised as follows:

- Holcim does not support separating a contract into separate performance obligations. Notwithstanding this fact, in considering whether a promised good or service is *distinct*, we believe that the definition proposed is too broad and consequently would include too many performance obligations especially with regards to construction contracts. This clearly will make the resulting accounting extremely complicated and difficult for users to understand.
- Holcim does not support the control model for revenue recognition. Notwithstanding this fact, we are concerned about the usefulness of the indicators included in the ED for determining whether control of a promised good or service has been transferred to a customer. Finally, it should be borne in mind that depending on the jurisdiction in which an entity is situated, transfer of control could occur at different times for the same transaction within a Group.
- Holcim does not believe that a customer's credit risk should be reflected as a reduction in revenue.
- Holcim believes that subsequent changes in the estimated transaction price should be allocated to different performance obligations based on facts and circumstances, rather than automatically in proportion to the initial stand-alone selling prices.
- Holcim does not consider that an entity should recognise a liability if a performance obligation included in an overall profitable contract is onerous.

To conclude, we strongly believe that the transfer of risks and rewards for the sale of goods and the percentage of completion method for construction contracts matches the underlying business substance and economics of a transaction. Therefore, any effort made to change and further complicate this approach will bring no additional benefit. On the contrary, it can only lead to a highly theoretical model that will confuse users of the financial statements.

Consequently, we believe that what is rather needed is an amendment to IAS 18 *Revenue* and IAS 11 *Construction Contracts* to provide further application guidance with respect to bundled contracts (i.e. contracts with more than one performance obligation) as opposed to a radical overhaul of the sound principles underlying the current revenue recognition model.

### **Holcim's responses to the questions asked in the exposure draft**

Holcim has a **fundamentally different view** as to what revenue is and when it should be recognised to the one proposed in the ED. However, rather than repeating this point throughout our responses to individual questions, **Holcim has chosen to answer the questions asked in the ED on the basis that the 'control model' for revenue recognition** – that revenue is recognised only when the customer obtains control over the good or service transferred by the entity – **would be applied**.

## **Recognition of revenue**

*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 for them as a single contract;*
- (b) to segment a single contract and 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 a contract modification as a separate contract?*

Holcim generally supports the concept of combining and segmenting contracts and contract modifications based on price interdependence which in substance is similar to the existing requirements in IAS 11 *Construction Contracts*. However, we believe that the ED should be clarified clearly explaining how that term should be interpreted and applied in practice.

*Question 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?*

**As already mentioned in our introductory paragraph, Holcim does not support separating a contract into separate performance obligations but if the IASB decides to pursue such an approach, our response to the proposal would be as follows:**

Holcim believes that the definition of distinct is too broad with a result that numerous performance obligations, particularly for construction contracts, will need to be accounted for separately if they are performed at different times. This clearly will make the accounting very complicated and difficult for users to understand.

*Question 3 — Do you think that the proposed guidance in paragraphs 25–30 and related application guidance is 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?*

**As already mentioned in our introductory paragraph, Holcim does not support the proposed control model for revenue recognition, as it believes that an activity-based model, under which revenue is recognised as the entity progresses towards the fulfilment of the contract, would result in more decision-useful information for users of the financial statements. This is especially the case for construction-related contracts which currently apply an activity-based model (i.e. percentage of completion method) for revenue recognition under IAS 11 *Construction Contracts*. However, if the IASB decides to pursue such an approach, our response to the proposal would be as follows:**

The ED includes a list of four indicators in order to provide examples of circumstances under which control often would be considered to have been transferred to the customer. It is therefore our understanding that an entity would always have to assess whether the contract and the relevant legislation provide the customer with control (that is, the ability to direct the use of, and receive the benefit from the good or service). We believe that there may be cases, in which control may not have been transferred even when all (or none) of the indicators stated in paragraph 30 are met. For example, control has not been transferred, even though all of the indicators have been met, when the seller has an unconditional repurchase option. Accordingly, it is our understanding that the indicators are nothing more than the impairment indicators in IAS 36, which do not offer conclusive evidence about the existence or absence of an impairment loss. Therefore, in order to avoid the indicators being used as a kind of checklist for when control exists, we believe that the role of the indicators should be clearly explained in order to avoid any confusion on this matter.

Finally, it should be borne in mind that depending on the jurisdiction in which an entity is situated, transfer of control could occur at different times for the same transaction within a Group.

### **Measurement of revenue**

*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 reasonably 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 criteria in paragraph 38? If not, what approach do you suggest for recognising revenue when the transaction price is variable and why?*

Holcim agrees that when the transaction price (or part of the transaction price) is variable, revenue should only be recognised if the transaction price can be measured reliably (or for the part for which it can be measured reliably). However, Holcim disagrees that the use of the expected value method would be appropriate in all circumstances.

In response to other discussion papers and exposure drafts from the IASB, we have often opposed to the use of probability-weighted amounts, especially in respect of single items. That is because, in our view, the use of the expected value method is appropriate only when applied to a large population of items (please refer more particularly to our comment letter on IAS 37 amendments dated 19.5.10).

*Question 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?*

Holcim does not agree that the customer's credit risk should be reflected as a reduction in revenue but rather should be recognized as an expense in profit or loss.

The primary reason for this is that users of financial statements usually find it useful if the revenue amount represents the quantity of goods or services sold multiplied by prices of these goods or services, and they usually consider a credit loss on a receivable separately. We understand that the main reason for this is that amounts related to credit losses have a different predictive value as they represent an estimate and require more judgement than the quantity of goods sold multiplied by their prices.

*Question 6 — Paragraphs 44 and 45 propose that an 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 agree with the proposal if the contract includes a material financing component.

*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?*

**As already mentioned in our introductory paragraph, Holcim does not support separating a contract into separate performance obligations but if the IASB decides to pursue such an approach, our response to the proposal would be as follows:**

Holcim agrees that the initial (estimated) transaction price should be allocated to all separate performance obligations in a contract in proportion to the stand-alone selling price. However, after the initial allocation, changes in the estimated transaction price should be allocated to different performance obligations based on the relevant facts and circumstances and not necessarily on the initial stand-alone selling prices.

### **Contract costs**

*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 specified criteria.*

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

#### *Costs of securing a contract*

In our view, if commissions and similar costs are incremental, necessary, directly related to a contract and will be recovered through the contract, they should be capitalised and not recognised as expenses when incurred. Holcim believes that the cash flows related to securing a contract are directly related to the contract and should therefore be accounted for as part of the contract. We believe that this is consistent with the current requirements in paragraph 21 of IAS 11 *Construction Contracts* in respect of costs incurred in securing a contract.

Furthermore, Holcim does not believe that it is appropriate that a revenue recognition standard should include requirements about costs incurred in fulfilling a contract. Instead, they should be included as consequential amendments in standards on IAS 2 *Inventories*, IAS 16 *Property, Plant and Equipment* or IAS 38 *Intangible Assets* respectively.

Apart from the comments above, Holcim believes that the requirements on accounting for the costs of fulfilling a contract are operational and sufficient.

*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 and why?*

#### *Capitalisation of costs*

Holcim agrees that an entity should apply the full direct cost method (i.e. including in the cost of an asset both incremental and allocated costs that relate directly to the asset) as suggested by the ED for measuring contract costs eligible for capitalisation.

However, as mentioned in our response to question 8 above, we also think that costs of securing a contract should be capitalised in certain circumstances.

#### *Onerous performance obligation versus profitable contract as a whole*

**As already mentioned in our introductory paragraph, Holcim does not support separating a contract into separate performance obligations but if the IASB decides to pursue such an approach, our response to the proposal would be as follows:**

Holcim does not believe it would be appropriate that a performance obligation is deemed onerous if the performance obligation is part of a contract that is profitable *as a whole*. We think that the proposed approach is inconsistent with the approach in IAS 37, which requires an entity to consider the unavoidable costs of meeting the obligations and the economic benefits expected to be received under the contract *as a whole*.

#### **Disclosure**

**As already mentioned in our introductory paragraph, Holcim does not support separating a contract into separate performance obligations but if the IASB decides to pursue such an approach, our response to the proposal would be as follows:**

*Question 10 — The objective of the boards' proposed disclosure requirements is to 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?*

While we agree that the purpose of the disclosures is to allow users to understand the amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers, we believe that the disclosures proposed are far too detailed. For example, disclosures required would include types of goods and services delivered, movement of contract balances and for contracts with a duration of more than one year, the amount of the allocated transaction price to be satisfied in time bands of one year.

We believe that such disclosures would significantly increase the costs of compliance in terms of system changes and audit procedures and add several more pages to the annual financial statements of multinational companies. Furthermore, it is not clear how the disclosures of a future IFRS on revenue recognition would overlap with those currently in IFRS 8 *Operating Segments*.

*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?*

As already mentioned in our response to question 10 above, we believe that such disclosures would significantly increase the costs of compliance in terms of system changes and audit procedures and add several more pages to the annual financial statements of multinational companies. In short, the costs of implementing such a disclosure proposal would far outweigh any benefits to be received as we seriously question whether it would provide added value to users of the financial statements.

*Question 12 — Do you agree that an entity should disaggregate revenue into the categories (e.g. major product lines or geography, such as country or region) that best depict how the amount, timing, and uncertainty of revenue and cash flows are affected by economic factors? If not, why?*

Holcim disagrees with the proposal as the required disclosures are already covered by IFRS 8 *Operating segments*. Since Holcim already voluntarily disclose information by product line in addition to information by reportable segment (i.e. by geography), we therefore believe that the proposed disclosure requirements are unnecessary.

### **Effective date and transition**

*Question 13 — Do you agree that an entity should apply the proposed requirements retrospectively (that is, as if the entity applied the proposed requirements to all contracts in existence at the effective date and in the comparative period)? If not, why?*

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

Holcim does not agree with retrospective application because we do not believe that the costs of restatement would justify any benefits because entities would be required to perform a complicated and cumbersome exercise of converting data of the previous financial year when the systems were not upgraded to collect the required information under the new standard. Therefore, this would involve manual intervention in order to retrieve the required data from thousands of contracts. As a consequence thereof, Holcim propose that the choice between prospective and retrospective application be left to the entities concerned.

## **Application guidance**

Question 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 proposal operational? If not, what additional guidance do you suggest?

While Holcim considers the application guidance useful, we believe that it should not form an integral part of the standard since it would render the future IFRS rule-based. Instead, we suggest that the application guidance be included for illustrative purposes only.

*Question 15 — The Boards propose 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?*

**As already mentioned in our introductory paragraph, Holcim does not support separating a contract into separate performance obligations but if the IASB decides to pursue such an approach, our response to the proposal would be as follows:**

We generally agree with the proposed distinction and accounting between the two types of product warranties.

*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 licence; 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 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?*

Holcim disagrees that a different accounting treatment should be applied depending on whether the right is exclusive (i.e. an entity *cannot* grant similar rights to other customers under substantially the same terms) or not. Consequently, we propose that the same

accounting treatment is applied to a licensing agreement regardless as to whether the rights are exclusive or not.

Holcim believes that revenue arising from a licensing arrangement should be recognized over the term of the agreement since the entity will be required to meet various contractual obligations of the contract (e.g. ongoing provision of technical assistance) over the license period.

### ***Consequential amendments***

*Question 17 — The boards propose that in accounting for the gain or 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 with the proposal.

We thank you for the opportunity to submit our contribution to your due process.

If you would like further clarification of the points raised in this letter, either of the undersigned would be happy to discuss these further with you.

**Keith Cameron**

Head Standards and Accounting Principles

**Raymond Meile**

Group IFRS Expert