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International Accounting Standards Board
30 Cannon Street
London
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United Kingdom

21 October 2010

By email to: commentletters@ifrs.org

Dear Sirs

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

I am writing on behalf of AFME (the Association for Financial Markets in Europe) to respond to the IASB's July 2010 Exposure Draft ED/2010/6: 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 on 1 November 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 broad range of participants in the wholesale financial markets. We welcome the opportunity to comment on this ED.

While it appears unlikely that the ED proposals will significantly affect our members, we would like to draw your attention to two concerns, which are set out in more detail in the responses below:

- The first concern is that we believe it is confusing to include credit risk in the measurement of revenue, and would strongly prefer credit risk to be addressed in measuring the receivable that arises at the point of recognition of the revenue earned. As a financial asset, we believe the impairment of the receivable should be addressed by the IASB's requirements for the impairment of financial assets (see our responses to Questions 5 and 6 below).

- A second concern arises over the clarity of the proposals regarding recognition of fees linked to the performance of, for example, an investment portfolio or price index (see our response to Question 4 below).

We set out below our detailed responses to certain of the questions on pages 11-15 of the ED; please note that we have not responded to all of these questions.

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

A significant issue for our industry is the recognition of performance fees in, for example, the investment management and private equity businesses, where fees may be linked to factors such as the return achieved on an investment portfolio.

We are concerned that Example 18 in paragraph B76 of the ED, which relates to management fees based on an index, could establish a precedent that such fees can never be reliably estimated, and hence recognised, until the performance condition is met. However, we find the rationale for the conclusion reached in this example to be unclear in the following respects:

i. The statement that "the entity determines that its experience with similar contracts is not relevant" could imply that experience with any contract which is based on market returns will be irrelevant, as past performance in financial markets is not necessarily a good indicator of future performance. We would disagree with any such implication, but the sentence should in any case be clarified.

ii. The example covers a fee which varies in line with the return achieved on the portfolio. We are not sure whether it is this variability which is deemed to preclude recognition of the performance element of the fee. A common alternative fee structure is that a fixed fee is received if performance exceeds a specified level – so if the target level is reasonably expected to be reached, it would seem reasonable to recognise the performance element of the fee at that time.

We therefore request the Board to clarify its intentions in relation to this example, either by clarifying the rationale for the conclusion in Example 18, or by providing additional examples to illustrate alternative scenarios.

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?

We do not agree that the customer's credit risk should affect the amount of revenue recognised by the entity. Revenue is a measure of the value of goods or services provided and it is not clear conceptually why, for example, identical services provided to two different customers would have different values because of the customers' different credit risks.

We believe it would be more appropriate for the ED to address solely the recognition of revenue (adjusted for discounts, rebates etc) but to exclude any adjustment for credit. Credit risk would not be incorporated in either the probability-weighted amount of expected revenue or within any applicable discount rate. The credit risk would however be taken into account when recognising the receivable at fair value on initial recognition and, subsequently, under the impairment rules for financial instruments. Initial recognition of the receivable would therefore continue to be at fair value, but there would be a clear distinction in the income statement between the revenue earned and the cost of any credit granted to the customer.

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?

Whilst we agree with reflecting the time value of money in the transaction price where material, we are concerned with the requirement in paragraph 45 to use "the rate that would be used in a separate financing transaction between the entity and its customer", which requires the inclusion of a credit spread within the discount rate. As discussed in our response to Question 5 above, we believe credit risk would be better dealt with through the impairment rules for financial instruments.

Question 10: The object 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 accepting that the proposed disclosure requirements will meet the stated objective, we note that these are substantially more extensive and detailed than the existing IAS 18 requirements. We suggest that the Board should carefully weigh the costs and benefits of the user community with those of preparers. In particular, we believe the proposed requirement to provide a reconciliation of contract balances would be too onerous, and would create undue cost without providing significant additional useful information to the users of financial statements.

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 disagree with the proposed requirement to disaggregate revenue into categories as we believe this disclosure would be too granular.

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 its better.

We agree with the proposal to apply the proposed requirements retrospectively, provided that sufficient time is allowed to implement the proposals.

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 proposals operational? If not, what additional guidance do you suggest?

As discussed in our response to Question 4 above, we believe additional guidance is required to clarify how the proposals should be applied to the recognition of fees linked to, for example, the performance of an investment portfolio.

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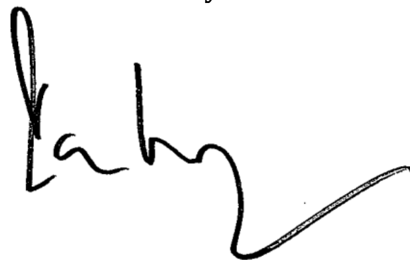
I hope the above comments are helpful. We would of course be pleased to discuss any points which you may find unclear, or where you believe AFME members might be able to assist in other ways.

Yours faithfully



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