Exposure-Draft Revenue from Contracts with Customers

Comments of UEPC

Presentation of UEPC

The European Union of Developers and House Builders (UEPC) represents more than 30,000 developing and house building companies, affiliated with its 12 member federations. Directly or indirectly the activities of these developers and house builders represent 10% of gross national product and employment in Europe. Together, they annually build and develop several millions m² of offices and shopping centres as well as more than 1.000,000 new homes.

Introduction

1. Before answering the questions put by the Exposure-Draft 2010/6, it would be helpful to consider whether all economic sectors indiscriminately should be subject to the new standards. Each one of them brings with them new burdens in terms of costs and energy, whereas measures are being taken willy-nilly to pull out of the economic crisis and avoid entering a new one.

The recovery requires resources and energy, and these could be deployed more effectively in this area rather than rolling out new accounting standards.

- 2. The more the standards applicable to all fields of activity are spelled out, itemising the way the standards are applied, the more we lose sight of the entity's actual activity, as it is increasingly unable to decide what adjustments are needed to apply the standard and paint a true picture of this activity.
- 3. The information overload highlights the vital need to leave it up to businesses to decide, under the supervision and responsibility of their auditors, what is and is not material for assessing the risks the entity runs carrying out its activity. All that is required to appreciate the truth of this is to examine the reports about the visits to internet sites offering financial information to entities.

A reference to this rule is justifiably made in paragraph 70.

Question 1 : Price interdependence for combining /segmenting contracts

1. The contract price interdependence criterion as a basis for deciding whether to *combine* contracts is not sufficient by itself: selling a piece of land and concluding a service contract to erect a building on this land should form a single contract, although the prices are not interdependent.

This is the economic objective of the contractor required to decide if what is involved is a single contract (the party would not have concluded one without the other) or otherwise.

- 2. Similarly, if a segmentation of contracts resulted from the entity being able to conclude each contract separately, this will invariably be the case for the sale of a house to be built. Several different contracts could actually be concluded to achieve this same objective: sale of land, design contract, project management, constructing the shell of a house, construction of technical installations, etc. This is not a sufficient reason to segment the single contract for the sale of a house at the planning stage.
- 3. There is no explicit link with the transfer of control: what point is there combining contracts if the control is changed at different times (such as the sale of land and the sale of a house to be built), the revenue from the combined contract should be segmented according to the date of the change of control.

Question 2 : Separate sale as a separate obligation criterion

It might be useful to add as a criterion, to justify that goods or services ensuing from the same contract are separate, the fact that the timetable for completing the activity is different. In the context of selling land with a building to be constructed, the land may be transferred immediately, while the construction is still pending.

Question 3: Transfer of control as a criterion for the completed activity

1. The IFRIC has already considered that the subject of the date created a problem for contracts transferring the ownership of a building to be constructed.

The D15 standard it has issued on this subject is not satisfactory. The Committee acknowledges its shortcoming, as, pursuant to national laws, it allows a rule that differs from the Completed Contract Method it imposes.

2. A rule for the sale of buildings to be constructed, comprising land and a structure, identical with other services and contracts, cannot be imposed. Imposing a single rule in this area runs the risk of creating information at odds with the legal situation of contracts, and the possibility that the information is found to be inaccurate.



- 3. Moreover, as the time spent building a property is subject to risks (tradespersons, supplies of materials, bad weather, etc.), if the revenue is recognised only when the control is transferred, the date is also uncertain and the information provided on this basis is not relevant because it is dependent on the event occurring a day prior to the information or a day after the information. The Percentage of Completion method does not allow for information whose relevance is constant.
- 4. The concept of the control of a property may be legal (the right to sell or mortgage, the burden of risk) or de facto (physical possession). The standard does not clearly show whether the revenue should be accounted for if the one transfer of control (legal) has taken place but not the other one (de facto).
- 5. There are legitimate grounds for wondering how the sale of a standardised product creates a different risk leading to a postponement of the recognition of the margin compared with a contract where the customer defines the product design.
- 6. Based on the purpose assigned to a building during construction, the margin it generates is not recorded if it is a stock, is recorded straight away if it is an investment, is recorded at the end of the construction process if it is sold and is recorded in line with the construction process if it is regarded as being covered by a construction contract.

This creates a major problem if the entity changes the purpose of the structure during construction or if it does not assign the same purpose to the entire structure.

- 7. Example 17 in the application guide (paragraph B 68) fails to illustrate the most common practice for selling an apartment (or another building) at the planning stage. In practice, an instrument (usually notarized) transfers the ownership before delivery. The payments are substantial during construction. The purchaser's possible entitlement to determine the item to be delivered may be much more extensive than the example specifies. What happens in this case?
- 8. By way of conclusion, the sale of a building to be constructed (residential or business) may take many commercial forms and be subject to many national laws governing this activity, often on a mandatory basis with a view to protecting the purchaser, hence it would be appropriate to leave it up to the entity to be free to choose to observe a Completed Contract Method rule or a Percentage of Completion rule, depending on whether one or the other method strikes the party as offering the most relevant information.

Should this approach not be accepted paragraph 31 should be reviewed with a view to fleshing it out and adjusting it.

Question 4: Price evaluation criteria

The criteria suggested in paragraph 38 are necessary and sufficient to allow the entity to make an entry in the accounts on the basis of the estimated price. Moreover, they also constitute the currently applicable rule.

Question 5: Credit risk related to recognition of the contract or solely the price

- 1. The customer's credit risk has to involve the question of the recognition of the contract, and should not affect how much revenue is to be recognised.
- 2. The credit risk should not/cannot be anticipated by a reduction of the recorded amount, because a necessarily more detailed evaluation of the risk to turn it into a reduction of the amount is impossible, as most customers do not have any rating and any sureties also have to be evaluated.
- 3. The evaluation of the risks via the recognised price would provide the accounts with a subjective element. It would be better to stick with the present criteria, such as the ageing schedule and litigation.

Question 6: Evaluation of future receivables

- 1. When the entity retains a receivable until its termination date, mainly because it is not redeemable, considering the financing cost via financial charges and discounting a receivable is tantamount to having the same financial charge appear twice in the entity's balance sheet.
- 2. Conversely, when the claim is securitisable, a market value may be established.

Question 7: Allocating the transaction price

- 1. The transaction price first of all has to be allocated according to the contract specifications:
- a) this is where the entity's legal obligations are laid down and b), the different prices in the contract represent the respective market values of the various obligations.
- 2. In the absence of a clear provision in the agreement, the proportional allocation proposed may be applied.

Question 8: Costs incurred fulfilling a contract

The provisions proposed for the costs incurred for fulfilling a contract are applicable and sufficient

Question 9: List of costs related directly to contract

The direct labour costs are not the only ones directly related to a contract. Mention may also be made of the management oversight costs that may be directly connected with a contract without it being a service provided to the customer. The expression "members of staff directly providing services to the customer" is therefore too restrictive.

Question 10: Information obligations

- 1. The information provided for in paragraph 75 (reconciliation of the opening and closing balances) is a purely accounting item offering no details about the operations of the entity. There is no point in disseminating this.
- 2. Qualitative rather than quantitative information about the sensitivity of the margin and the yields would help the reader to bring more focus to the entity's risk/profitability ratio and qualify the result of one period compared with the predictions for later periods.

Question 11: Information about the future

- 1. The information provided for in paragraph 78 and focusing on the price of transactions is irrelevant information.
- 2. More fundamentally, the information invokes the responsibility of the party providing the information. It may be normal for the management to assume responsibility for information about the past but it is inappropriate to ask the management to assume responsibility for information about the future, particularly the services delivery period. Calculating an entity's future forms part of the analyst's duties.
- 3. The information provided for in paragraph 77 offers sufficient indications.

Question 12 : Disaggregation of revenue

1. This disaggregation would involve a massive amount of work for some entities, without offering any genuine benefits for the reader.



2. Opting for the system of disaggregating revenue that best shows how the entity's operations are affected by economic factors provides an excessive element of subjectivity, that may discredit the information provided.

Question 14: Application guide

Example 17 in the application guide (paragraph B 68) fails to illustrate the most common practice for selling an apartment (or another building) at the planning stage.

In practice, an instrument (usually notarized) transfers the ownership before delivery. The payments are substantial at this time (the value of the land) and during the entire construction process. The purchaser's possible entitlement to determine the item to be delivered may be much more extensive than the example specifies.

Consequently, it is difficult to regard it as an application guide for the sector involving the sale of buildings at the planning stage.

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