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22 October 2010

Exposure Draft: Revenue from Contracts with Customers

Dear Mr Bement,

Deutsche Bank ("the Bank") would like to thank the IASB for the opportunity to comment on the Exposure Draft *Revenue from Contracts with Customers* ("ED").

We welcome the Board's efforts to develop a single principles based revenue recognition model that could be applied across all industries. Notwithstanding the above, we have the following comments for the Board's consideration in relation to the ED:

- With regards to revenue associated with financial instruments previously within the scope of IAS 18, for example, loan origination fees, loan commitment fees and guarantee fees, clarification is required as to whether these would fall into the scope of IFRS 9, IFRS 4 or under the ED. If the above named areas are to be included in IFRS 9, we would ask that the relevant sections of IFRS 9 be re-exposed. We would also recommend that the paragraphs in the current IAS 18 dealing with these items are left intact until the accounting is clarified.
- We do not agree with the proposed model where control is the sole determinant of recognising revenue. Rather we believe the existing model of IAS 18 of considering control and risks and rewards is more appropriate and is better aligned with the model for the de-recognition of financial instruments. Removal of any consideration of risks and rewards may result in transactions which are economically financing arrangements to be recorded as sales.
- We would further request clarification around the recognition of variable asset management fees and in particular to clarify that it is because the entity in Example 18 does not have history with the index that it is unable to reasonably estimate the revenue and that reliance on factors outside of management control, including market risk, would not be sufficient for management to be unable to determine a reasonable estimate of the revenue. Rather this should be done on a case by case basis.

- We strongly disagree with the proposed disclosures. In general we believe that the disclosure requirements should provide users with useful and relevant information. It is important that the Board carefully weighs the costs and benefits of the user community with that of the preparers. In our view, the disclosure requirement for a reconciliation of contract balances and of the performance obligations would be too onerous and only create undue cost without providing additional useful information to the users of financial statements. We further disagree with the proposed requirement to disaggregate revenue into categories as this disclosure would be too granular and is currently met by the current IFRS 8 disclosures. Furthermore, we would ask the IASB to consider whether these disclosures would provide useful information as it specifically relates to Financial Institutions.

The attached appendix includes the detailed comments in relation to the specific questions raised in the ED, which are significant to the Bank.

We hope you find our comments useful and relevant, and look forward to continue working with you in the future. Should you want to discuss in more detail the contents of the letter, please do not hesitate to contact Cynthia Mustafa at the following email address cynthia.mustafa@db.com and phone number 020 754 50978.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Cynthia Mustafa', written in a cursive style.

Cynthia Mustafa
Managing Director
Global Head, Accounting Policy and Advisory Group
Deutsche Bank AG

APPENDIX

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?

We agree with the principle of price interdependence.

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. Do you agree with that principle? If not, what principle would you specify for identifying separate performance obligations and why?

We agree with the principle of identifying performance obligations which are distinct; however, we disagree with the criteria provided as it relates to requiring a “distinct profit margin”. Because the other requirements would show “a standalone value” of the service/goods, we do not believe that the profit margin should be a criterion to demonstrate whether there is a distinct performance obligation. Therefore, we request that this be removed.

We believe that this would be practically difficult to implement especially in the financial services industry where revenue arrangements can often be bespoke in nature. In the financial services industry, revenue arrangements may often be unique to a specific client and transaction such that comparable data may not be available to assess whether the goods or services provided have a distinct profit margin. Therefore, we feel that the guidance in the current ED relating to this point would be practically difficult to implement.

Question 3

Do you think that the proposed guidance in paragraphs 25 – 31 and related application guidance are sufficient for determining when control of a promised good or service has been transferred to a customer? If not, why? What addition guidance would you propose and why?

We do not agree with the proposed model where control is the sole determinant of recognising revenue. Rather we believe the existing model of IAS 18 of considering control and risks and rewards is more appropriate and is better aligned with the model for the de-recognition of financial instruments. Removal of any consideration of risks and rewards may result in transactions which are economically financing arrangements to be recorded as sales. We are further concerned that there will be two significantly different models; control in Revenue Recognition and a mixed model of risk and rewards and control model for financial instruments,. We ask that the current guidance in IAS 18 for financial instruments be left intact until the Board reconsiders the IAS 39 derecognition model so that economically similar transactions are reported consistently.

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?

Performance based fees in the investment management business are significant to the Bank. We agree with the proposals that revenue should only be recognised when the transaction price can be reasonably estimated, but the proposals concern us for the following reasons:

1. By introducing the expected cash flow method, we are introducing uncertainty into the financial statements. As a practical matter it will be difficult and in certain cases arbitrary as to the estimates that entities will make. While we appreciate the need for investors to understand the uncertainties around revenue, we believe that this need is best served via the current disclosures around financial instruments in the financial statements.
2. Further clarification should be provided around the meaning of "experience". Particularly, as 38 (a) refers to the experience of other entities whereas paragraph b which only refers to the entity's own experience.
3. Paragraph 39 (c) further clouds the meaning of experience by including reference to a client's inexperience. Based on paragraph 38 (b) and 39 (c) therefore, unless an entity has previous experience with a particular contract, the transaction price cannot be reasonably estimated. If this is the Board's intention, we disagree with this principle. If not, we request that these paragraphs be clarified.

We would further request that the Board clarifies its intentions in relation to example 18, by providing additional examples to illustrate alternative circumstances. In particular to clarify that it is because the entity in Example 18 does not have history with the index that it is unable to reasonably estimate the revenue and that reliance on factors outside of management control, including market risk, would not be sufficient for management to be able to determine a reasonable estimate of the revenue. Rather this should be done on a case by case basis.

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 disagree with the use of the expected cash flow method, and we further disagree with the use of credit risk adjustments within the expected cash flow method, for the following reasons:

1. We would argue that the consideration of potential credit losses should form part of the impairment analysis, as this would relate to the collectability of a financial instrument, i.e. a receivable.
2. Users of the financial statements are likely to lose transparency as the "impairment" would form part of the revenue line, rather than as part of the impairment line item.

We would therefore ask that the credit risk should be considered within the Impairment project and that this be decoupled from revenue recognition. Additionally, this would create more transparency for users.

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 the concept of reflecting the time value of money where a contract includes a materially financing component, we disagree with the adjustment to the rate for credit risk as we are concerned that there may be "double counting" of credit risk by including the credit risk in both the expected cash flows and by adjusting the rate. As per question 5, we believe that credit risk should be addressed separately under the Impairment proposals, rather than as part of Revenue.

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?

We agree with the proposal in paragraph 50.

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?

We agree with the concept of recognising costs as revenue is earned but would like to highlight that we prefer the use of the words "direct and incremental costs" rather than considering direct labour, direct costs and indirect overhead costs. Direct and incremental are concepts which are currently understood today. Further we question the relevance of capitalising/recognising costs as assets prior to the contract being entered into.

Question 9

Paragraph 58 proposes the costs that relate directly to a contract for the purposes 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 or exclude and why?

As in Question 8, we ask for clarification around the allocation of costs which relate directly to the contract versus costs that were incurred only because the entity entered into the contract, as we understand these to be the same. We ask that the wording "direct and incremental costs" be included in 58 (c) and the removal of (e).

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?

In general, we believe that the disclosure requirements should provide users with useful and relevant information. We observe that the proposed disclosure requirements are substantially more extensive and detailed than the existing ones in IAS 18. Therefore, it is important that the Board carefully weighs the costs and benefits of the user community with that of the preparers. In our view, the disclosure requirement for a reconciliation of contract balances would be too onerous and only create undue cost without providing additional useful information to the users of financial statements. We further disagree with the proposed requirement to disaggregate revenue into categories as this disclosure would be too granular and is currently met by the current IFRS 8 disclosures. Furthermore, we would ask the IASB to consider whether these disclosures would provide useful information as it specifically relates to Financial Institutions.

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?

We strongly oppose the disclosure of this information as although we can see the rationale for this to certain industries we believe that this would not be relevant to the financial institutions. We are also concerned about the level of detail which may be required and believe that the needs of users of financial statements are met with the current disclosures surrounding the onerous obligations. We therefore believe that this should be an optional disclosure rather than a required disclosure.

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 believe this requirement is too granular and onerous for most financial services businesses. We believe the information currently required under IFRS 8, *Operating Segments*, would be sufficient to address the Boards' need for disclosure relating to revenue generated in different segments and from which type of customers. We would ask the Board to consider how the disclosures should be applied to financial services.

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 it is better.

Subject to our previous concerns raised about the inclusion of the credit spread and probability weighted information, we would agree with applying the requirements retrospectively in order to promote consistency between periods for users. However, we believe that sufficient time be 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?

Overall the application guidance provides adequate guidance as to the principles within the ED; however, we would appreciate more examples relating to the financial services industry. Subject to comments previously raised, we further have specific comments in relation to specific examples.

Example 1	An additional example showing the principle in relation to combining contracts into one would be useful.
Example 2	Scenario 2 focuses on the quantitative amounts but further guidance on why the principle has been met or not met would be useful.
Example 3	An example would be useful, and the impact on the balance sheet needs to be explained further. Would acting as an agent require a gross up on the balance sheet representing the respective contracts between the principal and the customer? It would appear that the guidance provided implies that the customer would be required to know that an entity is acting as an agent. Is this correct? If so, please include a specific sentence in the guidance to this effect.
Example 7	Although the example is a good example, it would be useful to provide further depth by detailing that the registration service is not providing a service in and of itself but is a necessary step in providing the service the client is actually paying for which is in relation to the gym membership. Further guidance around where for example a health screen is provided would be useful.
Example 8	We do not believe that the reference to IAS 17 should be made as intangible assets are no longer in the scope of the current leasing ED.
Example 14	Please provide a further example of where the sale and repurchase arrangement does not meet the sale requirements. Please further provide an example where a call is used and where the right to return or the call option is out of the money
Example 18	Clarify that it is because the entity does not have history with the index that it is unable to reasonably estimate the revenue and that reliance on factors outside of management control, including market risk, would not be sufficient for management to be unable to determine a reasonable estimate of the revenue. Rather this should be done on a case by case basis.
Example 19	Seems unduly complex and although consistent with the proposals we disagree with the proposals.

Example 26	This example could be better improved if other reference periods e.g. month 1, month 2, etc. are used as people may see reporting period as being one year.
Example 28	The guidance in paragraph 57 should be applied rather than only having the sentence "in accordance with 57".
Example 29	This example does not appear to be necessary as this appears to be duplicating principles already discussed.
Example 30	This should be titled "Presentation and Disclosure" please include examples of how we recognise performance obligations and whether we can show these on a net basis?
Example 31	Further include an example which deals with financial services.

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 that the sale of these goods should be consistent with the principles within the revenue recognition ED, however, this is subject to the comments we have made previously, specifically in relation to questions 3, 4 and 5.