



SAS Quadra 05. Bloco J. CFC
Brasília, Distrito Federal - Brazil

www.cpc.org.br

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International Accounting Standards Board

30 Cannon Street
London EC4M 6XH
United Kingdom

Financial Accounting Standards Board

401 Merritt 7, PO Box 5116
Norwalk, CT
06856-5116, USA

RE: Exposure Draft on Revenue from Contracts with Customers

Dear Sir/Madam,

The "Comitê de Pronunciamentos Contábeis" - CPC welcomes the opportunity to comment on the Exposure Draft named Presentation of Items of Other Comprehensive Income.

We are a standard-setting body engaged in the study, development and issuance of accounting standards, interpretations and guidance for Brazilian companies. Our members are nominated by the following entities:

- a) the São Paulo Stock Exchange;
- b) the Federal Accounting Council;
- c) the Brazilian Association of Listed Companies;
- d) the Brazilian Institute of Independent Auditors;
- e) the Research Institute of Accounting, Actuarial and Financial Foundation; and
- f) the National Association of Capital Market Investment Professionals and Analysts.

This response summarizes the views of our members, which may be supported by the opinions of external parties, sent to us for analysis and to enhance the discussion on the subject matter. We have also made efforts to encourage other external parties to send comments directly to the IASB.



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We would like to suggest that the Exposure Draft also clarifies whether the proposed statement would also be applicable for Small and Medium entities.

In addition, we enclose some specific comments from our member Brazilian Association of Listed Companies (ABRASCA) discussing the views of that entity in respect to the specific applicability of the Exposure Draft to the Real Estate industry in Brazil.

If you have any questions about our comments, please contact Silvio Takahashi (silvio.takahashi@br.ey.com).

Yours sincerely,

Edison Arisa Pereira

Technical Coordinator

Comitê de Pronunciamentos Contábeis (CPC)

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 (a) to combine or segment contracts and (b) to account for a contract modification as a separate contract?

Comments on Question 1

We understand that the purpose of combining contracts is valid, but indicators in paragraph 13 do not seem to be full determinant to the interdependency of prices, as they do not include the analysis of the substance of the contract.

We also agree with the concept of segmenting contracts. However, it is not clear how contracts will be segmented in practice based on the criteria included in the Exposure Draft, whenever the entity does not sell identical or similar items separately.

In respect to *contract modifications*, the Exposure Draft provides two different accounting treatments depending whether interdependency of prices are present or not in the contract. We believe that it is difficult to see when a modification would be independent of the original contract as, by its nature, the modification relates to the original contract. This situation is exacerbated in the industry that deals with long-term contracts, which usually presents several change orders requested by the customers, which would lead to increase or decrease in the contract revenue. However, we acknowledge that there might be certain situations where the contract modification changes significantly the original scope of the contract. In those cases, we believe that it might be appropriate the application of the proposed criterion included in the Exposure Draft.

Finally, we noticed that in several cases, the Exposure Draft only provides simplistic examples, which do not properly address the complexity of the entities 'actual environment (e.g., example 2)

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?

Comments on Question 2

We agree with the principle, however, the Boards should clearly determine the level of granularity needed, as many entities do have contracts with a large number of goods and services, might have difficulties in identifying the performance obligations. We suggest that the granularity would be set at the level of significant classes of performance obligations, usually aggregating similar obligations in one single category.

The standard does not clearly explain how performance obligations that are not distinct should be combined. We have particular concerns regarding how the tasks in Example 11 in the application guidance are combined. The example refers to a number of separate tasks (site preparation, foundation development, structure erection, piping, wiring, site finishing and contract management). Although all of the tasks could be obtained separately, the example concludes that foundation development, structure erection, piping, wiring and contract management must be combined because the contract management is not a separate performance obligation. The example does not explain why all of these tasks would be combined (as opposed to just two or three of them). Further guidance may be needed on when to combine tasks that are not performance obligations.

Finally, it might be difficult for the entities to determine whether a good or service is distinct when it is not sold separately. The Boards should also clarify why the indicator 23 (b) (ii), distinct profit margin would be an indicator that a good or service is distinct.

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 additional guidance would you propose and why?

Comments on Question 3

The application of the control principle is our key concern with the Exposure Draft. The indicators presented in paragraph 30 would not be applicable for all industries (e.g., services or software companies), whereas paragraph 31 does not provide guidance on how the entities would proceed in situations on which some indicators are not relevant. The discussion paper issued by the Boards in December 2008 provided more guidance to

the services industry, when mentioning the continuous transfer of control over services. Therefore, we would suggest that the Boards provide further guidance on how to determine the performance obligations and under what circumstances control can be considered to transfer continuously.

We also believe that the control definition presented in BC 63/BC 65 should be incorporated in the Exposure Draft for clarification purposes.

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

Comments on Question 4

The standard implies that a transaction price should be allocated to each performance obligation based on stand-alone selling price for each good and service. USGAAP ASU 2009-13 has established a hierarchy to determine individual prices (vendor-specific objective evidence, third-party evidence and lastly, estimated selling price), which was rejected by the Boards. We believe that the previous US GAAP approach would be more useful for applicants.

Whilst we understand the conceptual rationale for this approach, there are likely to be a number of practical issues. As there is no requirement for receipt of the consideration to be probable, there might be situations that will lead to including consideration in the transaction price although it may not be received (e.g only a 25% probability of receiving the consideration). We are concerned that this approach will require a high level of judgment to be applied and users may not expect such a judgmental amounts to be included in revenue. Proper and useful information about the level of judgement applied should be disclosed in notes to the financial statements.

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?

Comments on Question 5

We note that under IAS 18, revenue is recognised at fair value and, therefore, material credit risk issues should have been considered (although we do not consider that all entities have been applying this in practice under IAS 18). However, for US GAAP reporters this is a significant change, since the previous guidance for revenue recognition included the criterion that stated that “collectability is reasonably assured”. This change would mean that initial estimates of collectability will be treated as a deduction from revenue and subsequent changes as adjustments to other income/expense.

Overall, we agree with the proposed criterion of recognition of the credit risk. However, we note that, in some cases, there could be the need to improve the capabilities of the IT systems, since under the new model the credit risks need to be considered for all contracts up front.

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?

Comments on Question 6

We agree with the proposals, but the concept of what is a “material” financing component should be clearly defined in the final standard. In addition, the impact of foreign currency is not clear in the current Exposure Draft.

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?

Comments on Question 7

Refer to our response number 4 above. We agree conceptually but there are lots of practical difficulties. US reporters experience with ASC 605-25 has shown this can be difficult and costly to implement and the cost may outweigh the benefit. There are two key concerns:

- Can the entity actually do the calculations to determine all the different stand alone selling prices?
- Even if they can do the calculations, a number of entities might experience systems problems as systems may not cope with multiple prices for the same product sold to different customers (e.g. telecommunication companies)

How difficult this is in practice depends to some extent on the granularity of performance obligations identified (see response to question 2).

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?

Comments on Question 8

We agree conceptually, but we believe that such guidance should be provided in the standards related to inventory, property, plant and equipment, and intangible assets.

Amortization of contract costs should consider the period over the asset is expected to contribute to the cash flows of the entity, and not to the duration of the related contracts.

In addition, it might be difficult for some industries (e.g. construction) to track costs at a performance obligation level.

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?

Comments on Question 9

We agree with the costs specified, but believe that such matter should be addressed in the specific standards, meaning IAS 37 Provisions and ASC 450 Contingencies. In addition, we believe that entities will have difficulties by tracking onerous liabilities at the performance obligation level.

Disclosure

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?

Comments on Question 10

The level of disclosures required increased significantly, which might not provide useful information to the user of the financial statements, since some of them might not be used by the entities' management. In addition, IFRS 8 might be also revised to be consistent with the requirements of the Exposure Draft.

Disclosure requirements might be a challenge for more complex businesses, which normally have different types of contracts. A clarification on level of aggregation allowed should be useful (e.g., per reportable segment, per business line or others).

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?

Comments on Question 11

We agree with the proposed disclosure requirement, but as mentioned in question 2, aggregation criteria should be addressed in the standard. In some cases, if a defined criterion is not included in the Exposure Draft, it might involve significant level of judgment, which may not be auditable.

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?

Comments on Question 12

We agree, but as mentioned in our response to question 10, more clarification is required on the level of aggregation allowed. The boards should also define the meaning of affected by "economic factors". As mentioned earlier, IFRS 8 should also be amended

in order to be consistent with this standard.

Effective date and transition

Question 13

Do you agree that an entity should apply the proposed requirements retrospectively (ie 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.

Comments on Question 13

Although we conceptually agree with the proposals, we have concerns about full retrospective application, in particular for entities with existing long-term contracts, which would be required to retrospectively adjust for the proposed standard. We believe that a prospective approach would be adequate, with full disclosure of the changes in the notes to the financial statements.

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

Comments on Question 14

As mentioned earlier, some of the examples are overly simplistic and do not address the complexities in practice, including only a few indicators and criterion. Current existing guidance for specific industries under USGAAP should be analysed and incorporated in the application guidance (e.g. current software revenue recognition).

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?

Comments on Question 15

We conceptually agree, but question whether the current practice could be maintained. Additional guidance should be provided to explain the differences between the two types of warranties. Entities might also have difficulties in splitting a warranty contract where both types are offered.

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 it 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?

Comments on Question 16

We believe that the transfer of control to the customer is not determined by the exclusiveness of the licence, and do not believe that the revenue recognition pattern should be determined by such criterion.

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?

Comments on Question 17

Although we agree with the proposals, there is not sufficient guidance for such implementation. We raise two main questions: (i) how the variable portion of the transaction price (that could not be estimated) could be extended to the acquirer; and (ii) how to address the cases with no commercial substance.

Non-public entities

Question 18 [FASB only]

Should any of the proposed requirements be different for non-public entities (private companies and not-for-profit organisations)? If so, which requirement(s) and why?

Comments on Question 18

Jurisdictions should consider updating the local guidance for SMEs in order to align with the proposed model.

APPENDIX

ABRASCA COMMENTS IN RESPECT TO REAL ESTATE INDUSTRY IN BRAZIL

Recognition of revenue

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 additional guidance would you propose and why?

We suggest that, since control of good and service application is the core of Exposure Draft items 25-31, control transfer of goods not yet physically ready, but over which customer has all rights and control after contract signing, should be more explicit. Mostly, in regard of transfer of goods from the real estate sector, whose standard is interpreted by IFRIC 15, which did not represent the best way to interpret accounting information for the sector, in our country.

Thus, ABRASCA's Work Group of real estate developers went over each item from Exposure Draft items 25 to 31, under discussion hereto, and it realized that there is a need to change 3 items of the ED: item 30, letter c, item 30, letter d, and item 31. The major reason, already mentioned, is that these items do not explicit control transfer of goods that are not yet physically ready, but customer has all rights and control over the good after contract signing.

Therefore, in order to make the issue more comprehensive, we shall review each item from Exposure Draft items 25-31, with suggestion for change in the text of items 30, letter c; 30, letter d; and 31, as follows.

COMMENTS AND SUGGESTIONS OF CHANGES IN EXPOSURE DRAFT, QUESTION 3

ITEM 25

"25 An entity shall recognize revenue when it satisfies a performance obligation identified in accordance with paragraphs 20-24 by transferring a promised good or service to a customer. A good or service is transferred when the customer obtains control of that good or service."

Comments:

Developer transfers an asset to buyer at the sale act of an apartment, complying to item 25, and, consequently, in accordance to paragraphs 20 to 24.

The Brazilian real estate activity characteristics, as well as the legislation in force, mandate that developer or constructing firm to comply with certain requirements. These requirements give buyer, immediately, normally, the substantial rights over the good subject to contract, before the good or real estate is transferred physically to buyer.

The negotiation mode practiced by the Brazilian real estate market is defined by means of contract for sale and purchase or another form of contractual relationship between the developer and the buyer that can be changed entirely only by contract denouncing or amendment, respectively.

Real estate entrepreneur may alienate autonomous units (house, apartment, or business space) at three different instances: before initiation of works, during its construction, or, finally, after its completion. And as he is able to transform his unit in cash, it is possible to say that he has its control just after contract signature.

A significant majority of trading of undertakings takes place during the launching and construction process, therefore, prior to its full construction. Trading systematic occurs also, in majority of cases, within "set price" system, which is just the sales of units under global price contracting comprising fraction of the land and construction with set prices and deadline for delivery defined.

Concerning transfer of ownership, the signed contract has the power of a deed, and it may be taken immediately to register in the competent registry notary, assuring buyer all rights for free use of the good. It allows, mainly, for alienation of this good to a third party, its use as collateral for other contracts, etc. All it takes is seller's agreement if the good is financed by the incorporating firm itself (financial analysis).

Thus, developers comply to requirement of ED items 20-24, transferring the good to buyer in the act of selling this good, transferring the control of the good.

Ex:

Example of rights and obligations transfer of the good to buyer took place at the expropriation of a building occurring in undertaking still under construction. Developer was indemnified only for remnant units, not alienated yet, and each buyer was indemnified for his respective unit purchase according to a compromise of sale and purchase of the autonomous unit in the undertaking that was the subject of expropriation.

Thus, clearly characterizing transfer of rights, obligations, and risks of unit to each buyer, even though each buyer could not change acquired product during construction process.

ITEMS 26 and 27

"26 A customer obtains control of a good service when the customer has the ability to direct the use of, and receive the benefit from, the good or service.

Control includes the ability to prevent other entities from directing the use of, and receiving the benefit from, a good or service.”

“27 The customer’s ability to direct the use of a good or service (ie an asset) refers to the present right to use asset for its remaining economic life or to consume the asset in the customer’s activities, The customer’s ability to receive the benefit from an asset refers to its present right to obtain substantially all of the potential cash flows from that asset (either an increase in cash inflows or a decrease in cash outflows). The customer can obtain cash flows an asset directly or indirectly in many ways such as by using, consuming, selling, exchanging, pledging or holding the asset.”

Comments:

Developers comply to items 26 and 27 as already mentioned; there is, normally, immediate transfer of benefit of the good to buyer of the real estate who owns the rights over purchased asset.

When a customer decides to buy an unit of a certain undertaking, a house, a shop, or an apartment, the contract between developer and buyer is celebrated under the form of a compromise of purchase or sale or of a definite sale and purchase. This legal instrument (contract) has a commutative bilateral onerous feature, providing rights and obligations to both parties.

The right of use passes to buyer, who may sell, for example, the real estate even if it is not ready yet.

Ex: A customer buys a real estate in the drawing plant, in the beginning of works, for \$ 500 thousand. The building and, consequently, his apartment will be physically ready to live in two years. After 8 months from purchase, he becomes aware that there are interested people in buying his apartment for \$ 800 thousand, a valuation of \$ 300 thousand in just 8 months, and he decides to sell it. The buyer will assume all the rights that he has to sell the real estate as he has control over the good. Therefore, fulfilling a desire to get a financial profit of \$ 300 thousand.

ITEM 30, letter a

“30 An entity shall assess the transfer of control of goods or services for each separate performance obligation. Indicators that the customer has obtained control of a good or service include the following:

- a) The customer has an unconditional obligation to pay-if a customer is unconditionally obliged to pay for a good or service, typically that is because the customer has obtained control of the good or service in exchange. An obligation to pay is unconditional when nothing other than the passage of time is required before the payment is due.”*

Comments ITEM 30 , letter a:

Developers comply to item “a”, customers are unconditionally obliged to pay for a good or real state, transferring control to customer. Payment modalities include, cash payment in the act of purchase or through financing with set schedule.

Amounts paid by customers (purchasers) and/or liberated by financing agent are applied in the production of the undertaking, and they are not considered as advancement of funds as it happens in other markets practices in which amounts received from customers are unavailable to developer, in a security account, during project execution.

Usually, customer pays a value (down payment) and remaining amounts are paid monthly, which are part of the price directly paid to developer and, mandatorily, used in the production of said unit. If there is bank financing, amounts are disbursed directly to developer and applied in the production of the unit, as well.

ITEM 30, letter b

“30 An entity shall assess the transfer of control of goods or services for each separate performance obligation. Indicators that the customer has obtained control of a good or service include the following:

b) The customer has legal title-legal title often indicates which party has the ability to direct the use, and receive the benefit from, a good. Benefits of legal title include the ability to sell a good, exchange it for another asset, or use it to secure or settle debt. Hence, the transfer of legal title often coincides with the transfer of control. However, in some cases, possession of legal title is a protective right and may not coincide with the transfer of control to a customer.”

Comments ITEM 30 , letter b:

Developers comply to item “b”, as previously mentioned, when a customer decides to purchase an unit, i.e. a house, a shop, or apartment, the contract between developer and customer is celebrated under the mode of a compromise of purchase and sale or a definite contract for sale and purchase. This legal instrument (contract) is a legal bond that gives customer the right to usufruct the real estate, including the possibility of immediate sale, its exchange for another good and, objectively, the benefit of the good. That is, control is transferred to customer after the legal bond is celebrated.

The use right belongs now to customer, and he may even sell the real estate while it is not ready yet.

Ex: A customer buys a real estate in the drawing plant, in the beginning of works, for \$ 500 thousand. The building and, consequently, his apartment will be physically ready to live in two years. After 8 months from purchase, he becomes aware that there are interested people in buying his apartment for \$ 800 thousand, a valuation of \$ 300 thousand in just 8 months, and he decides to sell it. The buyer will assume all the right that he has to sell the

real estate as he has control over the good. Therefore, fulfilling a desire to get a financial profit of \$ 300 thousand.

ITEM 30 , letter c:

“30 An entity shall assess the transfer of control of goods or services for each separate performance obligation. Indicators that the customer has obtained control of a good or service include the following:

- c) The customer has physical possession-in many cases, the customer’s physical possession of a good gives the customer the ability to direct the use of that good. In some cases, however, physical possession does not coincide with control of a good. For example, in some consignment and in some and repurchase arrangements, an entity may have transferred physical possession but retained control of a good. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of a good that the customer controls.”*

Comments

Physical possession does not determine control in the case of the kind of good sold by Brazilian developers. Actually, we have the sale of a good to be delivered in the future in accordance to a project previously approved by basic legislation for the sector by municipal, state, and federal authorities. It may not be changed in its essence after signature of the compromise of purchase and sale, since units are developed in a vertical building. However, customer at signature starts to usufruct the good in its construction stage. He may alienate, inclusively, to third parties without developer’s agreement, except if this later provides financing for the new customer . The transfer of the good or its control happens even without its physical possession, since it is a good for future delivery.

However, there is transfer of ownership, signed contract has the power of a deed, immediately taken to registration in competent real estate registry, assuring customer all rights of free use of the good.

Developer uses resource directly gotten from customer and, mostly, funds from financing institutions by means of signing a financing contract of the endeavor between the developer and the financing institution for the development of the alienated good. The obligation of developer to build the undertaking remains, before the financing institution, in accordance to previously approved conditions and project that are submitted to evaluation by the financing institution. Mandatorily, the financing institution only disburses financing resources if there was a minimum sale percentage of units of the endeavor, since this sale constitutes payment collaterals for the financing, making it clear the existence of ownership transfer to third parties when developer alienates units to its customers.

Therefore, it is a fixed price contract in which the disbursement of funds targeted to construction is conditioned to “progress of works in percentage evidenced in the Endeavor Follow Up Report – ERA, according to physical-financial schedule approved by the financing

institution...”. This follow up, for disbursement purposes, “will be undertaken by financing institution’s engineering, been understood that inspection will be carried out exclusively for measuring progress of works and to check application of funds...”.

It is important to highlight that Brazilian legislation requires registration of security (contract) at the enrollment of the autonomous unit to materialize real right (of ownership or acquisition). However, with or without registration, the contract binds parties and it has liability power.

The major effect of a contract is to create a legal bond between parties, having as the first consequence “the bonding power of the contract”, which translates as non-retractable.

The contract, once perfect and finished, only is cancelled either by agreement of rescission (new bilateral manifestation of will) or by legal sentence.

This means that neither developer or customer, unilaterally, to untie from obligations yielded with the contract of purchase of the autonomous unit.

The duty for parties (developer and customer) to respect and abide the alienation contract for the autonomous unit derives, still, from “the social function of the contract”, because the contract is, above all, an economic phenomenon. Its major social function is to “serve for circulation of wealth, providing security to market flow”.

A regulatory example of the mandatory power of a contract of sale and purchase within the scope of real estate development: developer cannot change the project or deviate from the development plan, except with unanimous authorization of stakeholders or by legal requirement (Federal Law no. 4,591, article. 43, item IV). In the other hand, as it is a contract for sale of goods, customers have only a limited possibility to influence in the real estate, such as, the possibility to select a project from a range of options specified by the developer or to specify small variation in the basic project.

SUGGESTION FOR CHANGING THE TEXT

- c) The customer has physical possession-in many cases, the customer’s physical possession of a good gives the customer the ability to direct the use of that good. In some cases, however, the good is not already done physically but the control is with the customer before it, for example, in some real estate sales. In some cases, however, physical possession does not coincide with control of a good. For example, in some consignment and in some and repurchase arrangements, an entity may have transferred physical possession but retained control of a good. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of a good that the customer controls.

ITEM 30 , letter d:

“30 An entity shall assess the transfer of control of goods or services for each separate performance obligation. Indicators that the customer has obtained control of a good or service include the following:

d) The design or function of the good or service is customer-specific a good or service with a customer-specific design or function might be of little value to an entity because the good or service lacks an alternative use. For instance, if an entity cannot sell a customer-specific asset to another customer, it is likely that he would require the customer to obtain control of the asset (and pay for any work completed to date) as it is created. A customer’s ability to specify only minor changes to the design or function of a good or service or to choose from a range of standardized options specified by the entity typically would not indicate a customer-specific good or service. However, a customer’s ability to specific changes to the design or function of their good or service would indicate that a customer obtains control of the asset as it is created.”

Comments:

It is not simple to be able to change the project of a building or its apartments as there are engineering, densification of real estate development site, land occupation, environmental restrictions, and others as well. As previously stated, in Brazil, the majority of real estate development is sold before or during construction, and at this stage customer becomes owner or promising purchaser of an ideal fraction of the land and of facilities to be built.

Developer sell and customer purchases, in the purchase and sale at set price, a future unit duly specified in its descriptive features (private, common and total area, ideal fraction of land, location, internal division, descriptive memorial of specifications of project works, etc.).

There are instances that, due to marketing reasons, developer allows, under certain conditions, customer requests changes in the descriptive memorial or in the internal division of alienated unit by means of customization projects before beginning of works or even afterwards, as long as some minimum deadline is respected.

These conditions are extremely restrictive, due to practical (engineering, etc.) or legal reasons.

Customer will not impose, in absence of expressed contractual provision, on the developer the execution of such customization. (See legal opinions by Dr. Marcelo Terra).

However, as stated, the constraint is that the real estate developer, due to engineering restrictions, cannot accept certain changes desired by purchaser, such as the construction of a bigger balcony or a veranda, or a swimming pool, etc. Rather, there is possibility for small customizations, depending on the contract, in the interior of the apartment.

Even in case of sale of a ready unit, customer does not have condition to change the project, since it is inserted in a vertical building and its changes becomes unfeasible due to technical impossibility of implementing it. What happens at most in ready units are rehabilitations that do not change the essence of the product. It is possible to change internal measurements of spaces, for example, to enlarge living room, diminishing the bathroom, etc., but it is not possible to increase total area of the real estate or to develop a balcony.

Thus, relevant changes in the product does not occur in essence, either traded in the drawing plan or in a finished unit.

SUGGESTION OF TEXT

d) The design or function of the good or service is customer-specific a good or service with a customer-specific design or function might be of little value to an entity because the good or service lacks an alternative use. For instance, if an entity cannot sell a customer-specific asset to another customer or assets which are such a specialized nature that only the customer can use them without major modifications, it is likely that would require the customer to obtain control of the asset (and pay for any work completed to date) as it is created.

ITEM 31

“31 Not one of the preceding indicators determines by itself whether the customer has obtained control of the good service. Moreover, some indicators may not be relevant to a particular contract (for example, physical possession and legal title would not be relevant to services).”

Developers, aligned to previously stated, comply to item 31, but they highlight that, in the specific case, physical possession does not establish control of good. Thus, we suggest that text to include not only the features of services, but this non-relevance also in the real estate development.

SUGGESTION OF TEXT

“31 Not one of the preceding indicators determines by itself whether the customer has obtained control of the good service. Moreover, some indicators may not be relevant to a particular contract (for example, physical possession, and legal title would not be relevant to services and some real estate sales).

EXAMPLE 17 – SALE OF AN APARTMENT UNIT

To better illustrate the understanding described above, we prepared an example of a typical sale of an apartment unit, similarly to Example 17 of the Exposure Draft, page 64, currently in public hearing:

"The entity develops and performs the launching of a vertical building project, with sales of the units before the beginning of the construction, i.e., off-plan. The entity (real estate developer) at this point, is still the owner of a piece of land and of a construction project, which will be developed in such land. The units (apartments) are sold to clients by means of a purchase and sale agreement, which is irreversible and irretrievable. As from the moment of sale and signature of the agreement, the unit is no longer available to the real estate developer, and the related risks and benefits are transferred to the purchaser. The installments paid by the clients to the real estate developer, whether with their own resources or through bank financing arrangements, during the period of launching and construction of the project, are used by the real estate developer directly for costing of the construction. The purchase and sale agreement guarantees the purchaser control over the apartment, since, as mentioned above, the property could be sold (disposed of) by the purchaser after the agreement has been signed, in the applicable market. The unit does not need to be physically ready. The legal guarantee is the agreement, and the purchaser has control thereover as soon as the agreement is signed. During the construction period, the purchaser may modify the project of his unit (for example, floor, color etc.), provided the common project (building structure) is not changed and the deadline is not impacted. In such example, the purchaser obtains control as from the execution of the purchase and sale agreement, therefore before the unit is physically ready. Consequently, in this example, the client obtains control over the unit upon execution of the agreement, becoming the owner of an undivided interest in the land and future constructions therein, as the construction work takes place. Thus, the obligation of the real estate developer is completed as it constructs the sold unit. The client also obtains control over the unit, irrespective of its completion."