



12 March 2012

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Technical Director, File Reference No. 1820-100
Financial Accounting Standards Board
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Re: Exposure Draft – Revenue from Contracts with Customers

We are pleased to respond to the IASB and FASB (the ‘boards’) Exposure Draft, Revenue from Contracts with Customers, on behalf of PricewaterhouseCoopers. Following consultation with members of the PricewaterhouseCoopers network of firms, this response summarises the views of those member firms who commented on the exposure draft. 'PricewaterhouseCoopers' refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

We agree with the boards' objectives and support a single revenue recognition model that provides clearer and more consistent guidance. We also support the boards' efforts to respond to concerns raised by constituents on the original exposure draft, and commend the boards for their collaboration on this project which has led to the issuance of converged proposals.

We support the overall project. There are, however, areas where the concepts could be more clearly articulated, might be challenging to apply, or do not appear cost-beneficial. We explain these areas in our responses to the boards' questions in Appendix A and in the additional matters in Appendix B. We have also included responses to the FASB's questions on the US GAAP consequential amendments in Appendix C.

Our key comments and the more significant areas where we believe clarity could be added are explained below.

Performance obligations satisfied over time

We appreciate the boards providing additional principles to determine when a performance obligation is satisfied over time. We agree with the proposed criteria, as further discussed in our response to Question 1.

We agree that an asset having no alternative use is relevant in assessing when a performance obligation is satisfied over time. We disagree with including customer protective rights (such as contractual terms that preclude transfer to another customer) in defining when an asset has no alternative use. We are concerned that this might result in revenue recognition over time that does not reflect the economics of the transaction. The focus on customer protective rights to determine control is also inconsistent with IFRS and US GAAP consolidation guidance.



There should be greater clarity about whether a contract for the delivery of repetitive goods or services is a single performance obligation or multiple performance obligations. This might affect the pattern and timing of revenue recognition, the accounting for contract modifications, and the assessment of onerous performance obligations. We recommend the boards clarify how to determine the unit of account in these arrangements.

Variable consideration and 'reasonably assured'

We agree that the revenue an entity recognises for satisfied performance obligations should be limited to amounts for which the entity's experience is predictive of the consideration to which it will be entitled. We suggest the boards clarify that this assessment is intended to be qualitative and not a specific, quantitative threshold. We also suggest not using the term 'reasonably assured' in the standard, as this term is already used in certain existing guidance, is not interpreted consistently under IFRS and US GAAP, and such interpretations differ from the criteria in the exposure draft.

We do not believe an exception is needed for arrangements where the consideration for intellectual property licences varies based on a customer's subsequent sales. The proposed guidance sufficiently addresses sales-based royalty arrangements without the need for an exception.

The boards should clarify whether a change in the value of consideration received or receivable arises from a change to the transaction price (that is, variable consideration) or a remeasurement of an asset (for example, foreign currency remeasurements or changes in the value of non-monetary assets to be received). In our view, only changes arising from variable consideration should be reflected in revenue; other remeasurements should be recognised elsewhere in the income statement.

Onerous performance obligations

We disagree with including a requirement to assess whether a performance obligation is onerous, as it results in neither the recognition of incurred costs nor the recognition of revenue. We also believe the proposed accounting might not accurately reflect the economics of the arrangements, particularly when the entity obtains benefits beyond the consideration for the individual performance obligation or the contract.

We recommend that, if the assessment is retained, it should be performed at the contract level or higher, and that the wider economic benefits of the arrangement be considered. An entity might offer a good or service at a loss in a bundled arrangement because the arrangement as a whole is profitable. An entity may also knowingly enter into an unprofitable contract to supply goods or services because it is obtaining other benefits beyond the consideration from the customer (for example, an increase in market share).

We also disagree with the boards' view that the proposed scope limits the 'risk of unintended consequences' of applying the assessment because the proposed scope is close to existing revenue guidance. The proposed scope will capture a wide range of arrangements that are not subject to such an assessment under existing IFRS and US GAAP, such as services outside the scope of IAS 11 and ASC 605-35.



Disclosures

We believe that the proposal requires too many disclosures in both interim and annual financial statements, and recommend they be reduced. There is a risk that useful information will be obscured due to the volume of disclosures required. We also recommend that the disclosures be simplified. Reduced and simplified disclosures will better balance the needs of users and the burden on preparers.

We believe the proposed interim disclosures are inconsistent with the principle that interim reporting should reflect only significant changes since the last annual reporting period. The principles in existing interim reporting guidance should be considered to determine the extent of revenue disclosures required for interim financial statements.

Additional matters

Interaction with the proposed leasing standard – We encourage the boards to articulate any significant differences in the accounting models for licences of intangible assets and for leases of tangible assets. These arrangements are economically similar, and the boards should clearly explain any significant differences in the accounting models so that preparers and users understand the reasons. This will promote greater understanding of the guidance under the revenue and leasing standards.

Presentation of revenue – We acknowledge the boards' decision not to reconsider the definition of revenue in this project. We are concerned, however, that the proposals could create confusion about the composition of revenue. We suggest the boards clarify how entities should present revenue from contracts with customers and revenue from other sources. We also suggest the boards clarify the presentation of uncollectible amounts for different types of revenue.

Risk and rewards as an indicator of control – We agree with the principle that a performance obligation is satisfied when the control of a good or service is transferred to the customer. We also agree with the indicators of when control transfers, except that we recommend 'risks and rewards of ownership' not be an indicator. Entities might place too much emphasis on this indicator or focus on aspects of risks and rewards that do not reflect transfer of control. Retaining risk and rewards might indicate an additional performance obligation exists (for example, risk of loss during shipment) but would not necessarily indicate when control has transferred.

Economically linked arrangements – The requirement that only contracts with the same customer or related parties be combined might result in individual arrangements being accounted for separately even though they are economically linked. This could occur when goods or services are provided directly to the customer of an entity's customer. Consideration payable to a customer (or to other parties that purchase the entity's goods or services from the customer) should be accounted for as a reduction of the transaction price unless the payment is in exchange for a distinct good or service. The guidance should clarify that entities that provide a good or service as an incentive to a customer (or to parties that purchase the entity's goods or services from the customer in arrangements economically linked at the time of sale to the customer) should evaluate whether there is a performance obligation to which a portion of the transaction price should be allocated.



Time value of money – We understand the conceptual basis for adjusting the transaction price to reflect the time value of money if a contract includes a significant financing component. We remain concerned, however, that practical challenges will outweigh the benefit to users.

Transition – We appreciate the theoretical merit and potential benefit to investors of retrospective application to increase consistency across periods presented. The cost and effort involved in implementing this approach might, however, outweigh the benefits. We acknowledge the boards' efforts to reduce the challenges through practical expedients, but we believe opportunities exist to minimise the burden on preparers without significantly compromising the needs of users. We suggest that the standard allow entities to account for certain contracts prospectively if it is not practical to apply the standard retrospectively to those contracts.

If you have any questions, please contact John Hitchins, PwC Global Chief Accountant (+44 207 804 2497), Paul Kepple, PwC US Chief Accountant (+1 973 236 5293), Tony de Bell (+44 207 213 5336), or Brett Cohen (+1 973 236 7201).

Yours faithfully,

PricewaterhouseCoopers LLP



APPENDIX A

Question 1: *Paragraphs 35 and 36 specify when an entity transfers control of a good or service over time and, hence, when an entity satisfies a performance obligation and recognises revenue over time. Do you agree with that proposal? If not, what alternative do you recommend for determining when a good or service is transferred over time and why?*

We agree with the principles in paragraphs 35 and 36 to determine when a performance obligation is satisfied over time. The criteria proposed should address the majority of situations where revenue should be recognised over time.

We also agree that an asset having no alternative use is relevant in assessing when a performance obligation is satisfied over time. We disagree, however, with the proposed definition of when an asset has no alternative use as we believe it might lead to an unintended consequence and require that revenue is recognised over time as typical inventory items are manufactured in some situations. This is because the proposed definition considers customer protective rights (such as contractual terms that preclude transfer to another customer) as a determining factor of when an asset has no alternative use. The definition is inconsistent with recognising revenue when control transfers because customer protective rights do not determine control. It is inconsistent with the guidance in paragraph 37b, which states that retention of legal title solely as a protective right does not preclude a customer from obtaining control of an asset. It is also inconsistent with the consolidation guidance in IFRS 10 and ASC 810, which requires that investor-protective rights do not result in control over an investee.

Including customer protective rights in the proposed definition of when an asset has no alternative use might result in revenue recognition over time when this does not reflect the economics of the transaction. For example, the following might meet the definition of an asset with no alternative use:

- A contract that specifies the first car of a new model is for a particular customer.
- A contract that specifies the next 200 widgets produced are for a particular customer.

The car and widgets can be readily redirected to other customers if the customer cancels or breaches the contract. This puts pressure on the criteria in paragraph 35b (specifically 35b(iii)) to determine whether revenue should be recognised over time. This could result in unintended consequences for a typical inventory item just because it is contractually identified for a specific customer. Similar items might be accounted for differently based on the payment terms in the arrangement, with one treated as inventory and the other treated as a performance obligation satisfied over time as the item is manufactured. For these reasons, we suggest removing customer protective rights as an indicator of when an item has no alternative use.

The guidance on identifying separate performance obligations is unclear about whether a contract for the delivery of repetitive goods or services is a single performance obligation or multiple performance obligations. For example, a two-year contract for a daily cleaning service could be accounted for as a single performance obligation satisfied over time or daily distinct performance obligations. This determination might affect the following:

- Pattern and timing of recognition – The revenue recognised for each distinct performance obligation is determined by relative stand-alone selling prices, whereas revenue recognised for a single performance obligation satisfied over time is based on an output or input measure.



- Accounting for contract modifications – A contract modification is accounted for differently under paragraphs 22a and 22b, depending on whether the undelivered goods and services are distinct or part of a single performance obligation.
- Assessment of onerous performance obligations – The assessment is only required for performance obligations satisfied over time and over periods greater than one year. See our response to Question 4.

We recommend the boards provide greater clarity on how to apply the concept of ‘distinct’ to determine the unit of account in these types of arrangements.

Question 2: *Paragraphs 68 and 69 state that an entity would apply IFRS 9 (or IAS 39, if the entity has not yet adopted IFRS 9) or ASC Topic 310 to account for amounts of promised consideration that the entity assesses to be uncollectible because of a customer’s credit risk. The corresponding amounts in profit or loss would be presented as a separate line item adjacent to the revenue line item. Do you agree with those proposals? If not, what alternative do you recommend to account for the effects of a customer’s credit risk and why?*

We agree with the proposal to apply IFRS 9 or ASC 310 to account for consideration that might be uncollectible. The requirement to present the impact of credit risk on the face of the income statement in a line item adjacent to revenue is too prescriptive without providing additional benefit. Entities should be given the option to present this information in the notes. We comment further on the presentation of revenue in Appendix B ‘Definition of revenue and the customer.’

We also recommend including the principles in paragraphs BC174 and BC175 in the standard to clarify the guidance for the presentation of credit risk in a contract with a significant financing component.

Question 3: *Paragraph 81 states that if the amount of consideration to which an entity will be entitled is variable, the cumulative amount of revenue the entity recognises to date should not exceed the amount to which the entity is reasonably assured to be entitled. An entity is reasonably assured to be entitled to the amount allocated to satisfied performance obligations only if the entity has experience with similar performance obligations and that experience is predictive of the amount of consideration to which the entity will be entitled. Paragraph 82 lists indicators of when an entity’s experience may not be predictive of the amount of consideration to which the entity will be entitled in exchange for satisfying those performance obligations. Do you agree with the proposed constraint on the amount of revenue that an entity would recognise for satisfied performance obligations? If not, what alternative constraint do you recommend and why?*

We agree that an entity should be allowed to use either a probability-weighted or most-likely-outcome method to estimate variable consideration based on whichever is more predictive of the consideration to which it will be entitled.

We also agree that the revenue that an entity recognises for satisfied performance obligations should be limited to amounts for which the entity’s experience is predictive of the consideration to which it will be entitled. We suggest the boards clarify that the assessment of whether an entity’s experience is predictive is intended to be qualitative and not a specific, quantitative threshold.



We suggest not using the term ‘reasonably assured’ in the standard, as this term is already in use and is not interpreted consistently under IFRS and US GAAP. The term is currently a high quantitative threshold in applying US GAAP, specifically in assessing whether collectibility is reasonably assured in accordance with SEC SAB Topic 13. The term is also used in IAS 20, ‘Accounting for Government Grants’, and is a ‘probable’ or ‘more likely than not’ threshold, which is a lower threshold than under US GAAP.

We agree with the indicators in paragraph 82 for identifying when an entity’s experience might not be predictive of the variable consideration to which it will be entitled.

We therefore suggest the following to replace the guidance in paragraphs 81 through 83:

81. Where consideration is variable, the cumulative revenue recognised to date shall not exceed the amount for which the entity’s experience is predictive of the consideration to which it will be entitled. Predictive evidence might include the entity’s own experience or other objective evidence (where access to the experience of other entities exists).

82. An entity shall use judgement when evaluating whether its experience is predictive of the amount of consideration to which it will be entitled. This is a qualitative assessment that shall consider all relevant facts and circumstances.

83. Indicators that an entity’s experience (or other evidence) might not be predictive of the amount of consideration to which the entity will be entitled include, but are not limited to, the following:

(a) the amount of consideration is highly susceptible to factors outside the entity’s influence. Examples of those factors include volatility in a market, the judgement or actions of third parties, weather conditions, and a high risk of obsolescence of the promised good or service.

(b) the uncertainty about the amount of consideration is not expected to be resolved for a long period of time.

(c) the entity’s experience (or other evidence) with similar types of performance obligations is limited.

(d) the contract has a large number and broad range of possible consideration amounts.

The presence of any one of these indicators does not necessarily mean an entity’s experience (or other evidence) is not predictive of the amount of consideration to which the entity will be entitled.

An exception is not needed for licences of intellectual property with consideration that varies based on a customer’s subsequent sales. The principle above is sufficient to address sales-based royalty arrangements without the need for an exception. The proposed exception specific to sales-based royalties would also result in different outcomes for economically similar transactions. For example, trailing commissions received by an agent of an insurance company, as described in Example 14 of the exposure draft, have a different accounting outcome but are economically similar to sales-based royalties because they depend on the actions of third parties.



We recommend that the boards clarify how the revenue recognition constraint is applied to performance obligations satisfied over time. For example, an entity performs a service in exchange for fixed consideration of C2,000 and variable consideration of C1,000. The entity does not have predictive experience that it will be entitled to receive the C1,000 before completion. When performance is 50% complete, the proposals might be interpreted to require the entity to recognise either C1,000 (50% * C2,000), reflecting only the amount for which the entity has predictive experience or C1,500 (50% * C3,000) reflecting the entire transaction price. We believe that the recognition of C1,000 is a more accurate reflection of the principles of the model and suggest the boards include an example to clearly illustrate this.

We are concerned about the accounting for cost of goods sold when revenue recognition is constrained. Control of inventory transfers upon sale and the inventory is therefore derecognised. This would result in recognising cost of goods sold and the related revenue in a different period when the consideration is variable and constrained. This might not reflect the economics and profitability of the transaction. There is a similar issue in the accounting for some intellectual property licences with variable consideration. We acknowledge that the timing difference might be unavoidable given the constraint on the recognition of revenue when consideration is variable. Additional disclosure might be appropriate.

We also recommend the boards clarify whether a change in the value of consideration received or receivable arises from a change to the transaction price (that is, variable consideration) or a remeasurement of an asset. Consider three examples. An entity sells goods in exchange for a:

- Cash payment based on 1% of future sales of the customer.
- Cash payment in a foreign currency to be received at a future date.
- Cash payment based on a market price two months after delivery.

The cash payment based on future sales is variable consideration under the proposal. The payment in a foreign currency is a remeasurement of an asset, as the amount paid by the customer is fixed in the foreign currency. The treatment of the payment based on a market index is not clear. In our view, only changes arising from variable consideration should be reflected in revenue; other remeasurements should be recognised elsewhere in the income statement. We suggest adding the following language:

The value of the consideration to which an entity is entitled might change after the goods or services have transferred to the customer and revenue has been recognised. An entity shall assess whether these changes should be accounted for as a change to the transaction price in accordance with paragraphs 77-80, and thus be reflected in revenue, or as the remeasurement of an asset, which shall be accounted for in accordance with other relevant guidance and recognised outside of revenue.

The following might indicate that there is a remeasurement of an asset:

- *The amount of consideration is not variable from the customer's perspective (for example, the amount is fixed in the customer's currency, which differs from the functional currency of the receiving entity).*



- *The factor that leads to the remeasurement does not directly relate to the goods or services provided.*
- *The remeasurement is caused by circumstances outside the control of the entity or its customer (for example, changes linked to a market price or index).*

Question 4: *For a performance obligation that an entity satisfies over time and expects at contract inception to satisfy over a period of time greater than one year, paragraph 86 states that the entity should recognise a liability and a corresponding expense if the performance obligation is onerous. Do you agree with the proposed scope of the onerous test? If not, what alternative scope do you recommend and why?*

We disagree with including a requirement to assess whether a performance obligation is onerous, as it would result in neither the recognition of incurred costs nor the recognition of revenue. The proposed accounting might not reflect the economics of the arrangements, particularly when the entity obtains benefits beyond the consideration for the individual performance obligation or the contract.

We recommend that, if the assessment is retained, it should be performed at the contract level or higher, and the wider economic benefits of the arrangement be considered. An entity might offer a good or service at a loss in a bundled arrangement because the contract as a whole is profitable. An entity may also knowingly enter into an unprofitable contract to supply goods or services because it is obtaining other benefits beyond the consideration from the customer (for example, an increase in market share).

We also disagree with the boards' view that the proposed scope limits the 'risk of unintended consequences' of applying the assessment because the proposed scope is close to existing revenue guidance in IAS 11 and ASC 605-35. The proposed scope will capture a wide range of arrangements that are not subject to such an assessment under existing IFRS and US GAAP, as most long-term service arrangements are not in the scope of IAS 11 or ASC 605-35.

Assessing performance obligations each reporting period to determine whether they are onerous will be challenging for many entities. Costs might not be tracked at the performance obligation level; therefore an assessment of whether performance obligations are onerous could be more challenging than an assessment at the contract level or higher. We do not believe the benefits of making an assessment at the performance obligation level will outweigh the cost or effort.

The proposals also make determining the unit of account (that is, whether there is a series of distinct performance obligations or a single performance obligation satisfied over time) important when it might otherwise have a limited impact on the recognition and measurement of revenue. For example, an entity enters into a two-year contract to provide a daily security service for an office building. The entity could apply the criteria in paragraphs 35 and 36 to the contract as a whole and recognise revenue over the two-year contract in a pattern that best depicts performance. The entity could also account for this contract as 730 distinct performance obligations, one satisfied each day the service is performed. The resulting pattern of revenue recognition would likely be similar in both cases but the entity which accounted for the contract as multiple performance obligations would not be required to consider whether there is an onerous performance obligation at each reporting period.



Question 5: *The boards propose to amend IAS 34 and ASC Topic 270 to specify the disclosures about revenue and contracts with customers that an entity should include in its interim financial reports. The disclosures that would be required (if material) are:*

- *The disaggregation of revenue (paragraphs 114 and 115)*
- *A tabular reconciliation of the movements in the aggregate balance of contract assets and contract liabilities for the current reporting period (paragraph 117)*
- *An analysis of the entity's remaining performance obligations (paragraphs 119–121)*
- *Information on onerous performance obligations and a tabular reconciliation of the movements in the corresponding onerous liability for the current reporting period (paragraphs 122 and 123)*
- *A tabular reconciliation of the movements of the assets recognised from the costs to obtain or fulfil a contract with a customer (paragraph 128).*

Do you agree that an entity should be required to provide each of those disclosures in its interim financial reports? In your response, please comment on whether those proposed disclosures achieve an appropriate balance between the benefits to users of having that information and the costs to entities to prepare and audit that information. If you think that the proposed disclosures do not appropriately balance those benefits and costs, please identify the disclosures that an entity should be required to include in its interim financial reports.

The proposed interim disclosures are inconsistent with the principle that interim reporting should reflect only significant changes since the last annual reporting period. The principles in IAS 34 and ASC 270 should be considered to determine the extent of revenue disclosures for interim financial statements.

The proposal also requires too many disclosures in both interim and annual financial statements, and there is a risk that useful information will be obscured due to the volume of disclosures that would be required. Simplified or reduced disclosures will better balance the information needs of users and the burden on preparers.

We believe the most important disclosures for annual financial statements are:

- A description of the principal sources of revenue and the accounting policies applied to each significant revenue stream.
- A description of the significant estimates and judgements made in recognising and measuring revenue and the extent to which revenue in the current period is affected by changes in those estimates and judgements.
- A quantitative analysis of the revenue derived from each principal source, disaggregated to depict how the amount, timing, and uncertainties of revenue and cash flows are affected by economic factors.

We recommend the boards reconsider the following proposed disclosures:

- *Disaggregation of revenue* (paragraphs 114-116) – This disclosure should reflect the information about revenue that is used to manage the business, consistent with segment reporting guidance, and should not duplicate segment disclosures.



- *Reconciliation of contract balances* (paragraph 117) – The objective of this disclosure is unclear, and we do not believe it provides decision-useful information, especially when an entity collects cash or records receivables immediately upon satisfying a performance obligation.
- *Performance obligations* (paragraphs 119 – 121) – An analysis of the entity's remaining performance obligations does not provide decision-useful information in all situations and might be burdensome to preparers. For example, these amounts would not include all components of an entity's backlog and would provide only partial information to investors. Many preparers could be required to develop systems to capture the information solely for the purpose of this disclosure. We recommend removing the disclosure requirement, but if retained, the boards should clarify that it excludes performance obligations that have been satisfied even if revenue recognition has been constrained.

We agree with the simplified approach to and reduced disclosures for non-public entities under US GAAP.

Question 6: *For the transfer of a non-financial asset that is not an output of an entity's ordinary activities (for example, property, plant and equipment within the scope of IAS 16 or IAS 40, or ASC Topic 360), the boards propose amending other standards to require that an entity apply (a) the proposed requirements on control to determine when to derecognise the asset, and (b) the proposed measurement requirements to determine the amount of gain or loss to recognise upon derecognition of the asset. Do you agree that an entity should apply the proposed control and measurement requirements to account for the transfer of non-financial assets that are not an output of an entity's ordinary activities? If not, what alternative do you recommend and why?*

The boards currently have different derecognition models and measurement guidance depending on the item in question. For example, under US GAAP, the existence of a legal subsidiary or the nature of the asset, including whether it is held in an incorporated entity, results in specific conclusions in many instances. The FASB recently added a research project on this topic. It is unclear how the boards would address such scope issues under this guidance. We recommend the scope of the guidance be clear if the boards move forward with this aspect of the proposal.

Assuming these scope issues can be resolved, we agree with the proposal to amend other standards for the transfer of a non-financial asset that is not an output of an entity's ordinary activities. We agree that an entity should apply the proposed requirements on transfer of control to determine when to derecognise the asset. We also agree that an entity should apply the measurement requirements from the standard to determine the amount of gain or loss to be recognised upon derecognition of the asset. We have explained in the response to Question 3 our concern that the requirements of the standard might not reflect the economics of a transaction and its profitability when the consideration is constrained. The boards should also consider these comments in the context of amending the guidance for the transfer of non-financial assets.



APPENDIX B – ADDITIONAL MATTERS

We have included our comments below on other significant matters in the exposure draft where we believe the concepts could be further clarified, might be challenging to apply, or do not appear cost-beneficial.

Scope

We support recognising revenue for licences when control of the right to use the intellectual property transfers to the licensee. Licences of intangible assets and leases of tangible assets are economically similar, so the boards should clearly articulate any significant differences in the accounting models to ensure that preparers and users understand the reasons. This will promote a greater understanding of the guidance under the revenue and leasing standards.

The proposed standard excludes ‘... non-monetary exchanges between entities in the same line of business to facilitate sales to customers other than the parties to the exchange...’. We continue to disagree with this exclusion. Non-monetary transactions should be excluded only if they lack economic substance.

We note that paragraphs 104-106 require an asset to be recorded when an entity has a right to receive consideration. This is consistent with financial instruments guidance, but we have the following concerns:

- It is unclear how this requirement interacts with the constraint on revenue recognition described in paragraphs 81-85. Recording an asset for the right to variable consideration that is constrained is inconsistent with the proposed accounting for revenue. This would also result in an entity recording a liability for which it has no obligation.
- Paragraph 104 could be seen as inconsistent with paragraph 15, which states that no accounting is required for wholly unperformed contracts. An entity might have an unconditional right to receive cash before either party has performed under the arrangement (for example, the right to invoice an up-front fee).

We recommend that the boards clarify that no asset or liability should be recorded until revenue is no longer constrained or one of the parties has performed (for example, if the entity receives a cash payment from the customer prior to revenue recognition). We also recommend that an entity disclose the expected effects of such transactions.

Definition of revenue and the customer

We agree that the definitions of revenue in the revenue standard and the conceptual framework should be consistent. We are concerned, however, that the proposals could create confusion about the composition of revenue. We suggest that the boards clarify how entities should present revenue from contracts with customers, revenue from other sources, and the impact of credit risk.

The definition of a customer is important in determining whether a contract is in the scope of the revenue standard. We therefore recommend that the boards provide indicators to promote consistency in how the definition of a customer is applied. We recommend the boards replace paragraph 10 with the following:



A customer is a party that enters into a contract with an entity to obtain goods or services that are an output of the entity's ordinary activities. The proposed guidance applies only to a contract (other than a contract listed in paragraph 9) where the counterparty to the contract is a customer. For some contracts, the counterparty to the contract might not be a customer but rather a collaborator or a partner. Indicators that a collaborator or partner relationship might exist, rather than a customer relationship, include but are not limited to:

- *The parties share the risks and benefits of the commercial success of bringing a good or service to market.*
- *The parties are active participants in directing and carrying out the activity of bringing a good or service to market. Active participation might be evident through the exercise of contractual or legal rights or business practice.*
- *The parties collectively control the arrangement and mutually benefit from it.*

Economically linked arrangements

The requirement that only contracts with the same customer or related parties can be combined might result in individual arrangements being accounted for separately even though they are economically linked. For example, a manufacturer sells a good to a distributor but provides a good or service to the distributor's customer at no additional charge as part of an arrangement economically linked at the time of sale to the distributor. The proposed guidance could be interpreted to prevent the manufacturer from allocating revenue to the additional good or service and thus preclude accounting for these transactions together in accordance with their economic substance. For these reasons, we propose the following modifications to paragraph 17:

17 An entity shall combine two or more contracts, whether with a single customer, a group of customers, or other parties that purchase the entity's goods or services from the customer, entered into at or near the same time with the same customer (or related parties) and account for the contracts as a single contract if one or more of the following criteria are met:

- (a) the contracts are negotiated as a package with a single commercial objective;*
- (b) the ~~amount of~~ consideration to be paid in one contract depends on the price or performance of the other contract; or*
- (c) the goods or services promised in the separate contracts (or some goods or services promised in the contracts) are a single performance obligation in accordance with paragraphs 27–30.*

Entering into separate contracts with the same entity (or related parties) at or near the same time might indicate that one or more of the criteria above are met.

The accounting for consideration payable to a customer should reflect a similar principle. Consideration payable to a customer (or to other parties that purchase the entity's goods or services from the customer) should be accounted for as a reduction of the transaction price unless the payment is for a distinct good or service. Entities that provide a good or service as an incentive to a customer (or to other parties that purchase the entity's goods or services from the customer in an arrangement



economically linked at the time of sale to the customer) should evaluate whether there is a performance obligation to which a portion of the transaction price should be allocated. We recommend the following modifications to paragraph 65:

65 Consideration payable to a customer includes amounts that an entity pays, or expects to pay, to a customer (or to other parties that purchase the entity's goods or services from the customer) in the form of (a) cash, (b) credit, or (c) other items (for example, a coupon, voucher or other 'cash-like' items) that ~~the customer~~ can be applied ~~apply~~ against amounts owed to the entity (or to other parties that purchase the entity's goods or services).

65A An entity shall account for the consideration described in paragraph 65 as a reduction of the transaction price and, hence, of revenue unless the payment to the customer is in exchange for a distinct good or service (as described in paragraphs 28 and 29) that the customer transfers to the entity.

65B Incentives provided to a customer (or to other parties that purchase the entity's goods or services from the customer in an arrangement that is economically linked at the time of sale to the customer) might be in the form of a good or service. The entity shall evaluate whether the good or service is a performance obligation as described in paragraph 24 and thus whether a portion of the transaction price should be allocated to it under paragraph 70. The entity shall consider the guidance in paragraph 17 to determine whether any performance obligation(s) identified should be combined with an existing contract with a customer (or other parties that purchase the entity's goods or services from the customer).

The proposal is not clear about the interaction between the guidance on costs to obtain a contract and consideration payable to a customer. For example, an entity might make a payment to a customer to enter into a customer-vendor relationship. We believe this payment should be capitalised as a cost to obtain a contract, assuming it meets the criteria in paragraph 94. Amortisation of this asset, however, should be recorded as a reduction of revenue in accordance with paragraph 65. We recommend the proposal specify the accounting for these arrangements.

Identification of separate performance obligations

We agree that distinct performance obligations should be identified and accounted for separately. We also agree with the criteria to determine when a performance obligation is distinct. We believe the guidance in paragraph 29 is helpful to determine whether a bundle of otherwise distinct goods or services might not be distinct and should be accounted for as a single performance obligation.

We are concerned that the term 'notwithstanding' in paragraph 29 removes the application of judgement to determine whether a bundle of goods or services should be accounted for as a single performance obligation or as separate distinct performance obligations. There might be circumstances where the goods or services are distinct yet also highly interrelated or significantly customised. The principle should allow entities to make judgements to enable the accounting to reflect the underlying economics of the transaction. We suggest amending paragraph 29 as follows:

Notwithstanding the requirements in paragraph 28, a Goods or services in a bundle of goods or services that otherwise meet the criteria in paragraph 28 is ~~is~~ might not be distinct in some circumstances and, therefore, the entity ~~shall~~ might account for the bundle as a single



performance obligation. Indicators that goods or services in a bundle might not be distinct include if both of the following are met:

- (a) The goods or services in the bundle are highly interrelated and transferring them to the customer requires that the entity also provide a significant service of integrating the goods or services into the combined item(s) for which the customer has contracted; and*
- (b) The bundle of goods or services is significantly modified or customised to fulfil the contract.*

It would also be helpful if the boards clarify whether other arrangements create a separate performance obligation, such as a promise not to do something (for example, a non-compete agreement) or an agreement to change the terms of a contract (for example, reservation change fees). An entity should apply the criteria in paragraphs 23 through 30 to identify separate performance obligations. In many cases, the result will be that these types of activities are not identified as separate performance obligations. In our view, a promise not to do something would typically not meet the definition of a performance obligation. A fee for agreeing to change the terms of a contract, for example, a reservation, does not satisfy the 'distinct' requirement and should be accounted for in accordance with the contract modification guidance.

Paragraph 26d provides when-and-if available products as an example of a stand-ready obligation. We believe unspecified products promised on a when-and-if available basis are similar to stand-ready obligations that are satisfied over time, whereas specific products, even if promised on a when-and-if available basis, are similar to distinct performance obligations generally satisfied at a point in time. We suggest the boards clarify paragraph 26d accordingly.

Customer options

We agree with the proposed model to account for customer options, which requires revenue to be allocated to a right that the customer would not have received without entering into that contract. We recommend that the term 'material' be deleted as rights that are individually immaterial but collectively material, such as customer loyalty points, create performance obligations.

We also believe the guidance for cancellation or renewal options requires clarification when there are no future performance obligations, such as in a licence arrangement. Paragraph B24 allows entities to consider renewals to determine and allocate the transaction price in an arrangement when there is a material right. An entity that concludes there is a material right and makes use of the practical expedient will record revenue for the initial term and the renewal periods when control of the licence transfers. An entity that concludes there is no material right cannot use the expedient and will recognise revenue only when the renewal options are exercised. We believe that this accounting reflects the economic substance of these arrangements if the material right provides a significant economic incentive to exercise the option. We recommend, however, that the boards clarify that:

- The practical expedient in paragraph B24 is limited to situations where the customer has a significant economic incentive to exercise the option (due to our proposed deletion of the word 'material' above); and



- The recognition of revenue would be constrained to amounts for which the entity's experience is predictive of the amount to which it will be entitled in accordance with paragraph 81.

We also recommend that the principles in paragraph BC300 focus on the economic substance of cancellation and renewal options to avoid the implication that these are always interchangeable. For example, a contract that can be cancelled without penalty might be economically similar to a renewal option but a contract with a material right to renew or a contract that can be cancelled only with a penalty might be economically different.

Time value of money

We understand the conceptual basis for adjusting the transaction price to reflect the time value of money if a contract includes a significant financing component. We remain concerned, however, that practical challenges will outweigh the benefit to users. Example 9 demonstrates that even in a basic transaction the computations can be complex and require entities to make significant changes to systems and processes. Entities might find it difficult to assess the timing of delivery of goods and services relative to the timing of cash payments to determine if a significant financing component exists in certain transactions. Other examples that might be complex or even counterintuitive include:

- Long term contracts or multiple element arrangements where consideration is received throughout the performance period and performance occurs over time;
- An upfront fee received for a service provided over an extended period of time; and
- Performance obligations satisfied upfront where consideration is received over a long period of time and is not 'reasonably assured' at inception, which would result in interest income being recognised in advance of revenue.

We appreciate the boards' efforts to limit the challenges by providing indicators to determine when a significant financing component exists. We agree with these indicators and recommend the boards consider an additional indicator based on how an entity manages its net cash flows in an arrangement.

We also recommend bringing forward into the standard or implementation guidance the concept in paragraph BC144 that goods or services that are available to the customer upon request (for example, customer loyalty points) do not include a significant financing component.

Allocation of the transaction price

We agree with allocating the transaction price to separate performance obligations based on their relative stand-alone selling prices. We also agree with the use of the residual approach in circumstances when the stand-alone selling price of a performance obligation is 'highly variable' or 'uncertain.' We have concerns, however, that the residual approach could be confused with the residual method that has been used in some situations historically to allocate transaction price.

We suggest the boards clarify that the residual approach is a means of estimating the stand-alone selling price, rather than an allocation methodology, so that discounts are appropriately allocated. The approach should only be used when other methods are not available. This can be made clearer by



moving the description of the residual approach in paragraph 73c to a separate paragraph, amended as follows:

If observable inputs are not available and if the stand-alone selling price of a good or service is highly variable or uncertain, then an entity may estimate the stand-alone selling price by reference to the total transaction price less the sum of the observable or estimated stand-alone selling price of other goods or services promised in the contract (inclusive of any discounts specifically allocated in accordance with paragraph 75). A selling price is highly variable when an entity sells the same good or service to different customers (at or near the same time) for a broad range of amounts. A selling price is uncertain when an entity has not yet established a price for a good or service and the good or service has not previously been sold. The residual approach should be used solely to develop an estimate of the stand-alone selling price of the separate good or service when there is a discount in the arrangement, and not to derive the amount allocated to each performance obligation.

Recognising revenue

Indicators of control

We agree with the principle that a performance obligation is satisfied when a good or service is transferred to the customer. We also agree with the indicators of when control transfers, except that we recommend 'risks and rewards of ownership' not be an indicator. The other indicators are objective while this indicator is inherently subjective. Entities might place too much emphasis on this indicator or focus on aspects of risks and rewards that do not reflect transfer of control.

Retaining risks and rewards might indicate an additional performance obligation(s) exists (for example, risk of loss during shipment) but would not indicate when control has transferred. We suggest deleting 'risks and rewards of ownership' as an indicator and adding the following paragraph after the indicators in paragraph 37:

When one or more of the indicators above point to control having been transferred to the customer, but significantly all the risks and rewards of ownership of the good or service remain with the vendor, this might indicate that the entity has an additional performance obligation(s) or that the transaction price might need to be adjusted.

Revenue recognition over time

We agree that the objective of measuring revenue over time is to depict the transfer to the customer. We disagree, however, with the exception in paragraph 46, which limits the revenue recognised on uninstalled materials to the cost of the materials, because it is inconsistent with the principles in the model. For example, the guidance in paragraph 46 results in accounting that is different if the entity constructs a large component rather than subcontracting the construction of that same component. If the entity were to construct the specialised equipment itself rather than purchasing it from a third party, it could recognise profit on the equipment as it is constructed.

We note the boards' concern that revenue will be recognised too early in some circumstances. We believe that the proposals (including paragraphs 38, 39, and 45) provide adequate guidance to determine the measure of progress and to limit that measure to what depicts transfer to the customer.



We believe that this could be enhanced by an example to demonstrate when revenue should not be recognised because uninstalled materials do not depict transfer of control to the customer.

Repetitive goods or services transactions

Some entities enter into a contract to deliver repetitive goods or services where the contract establishes a price per unit that increases or decreases over time. The proposed guidance on calculating stand-alone selling price and measuring progress towards completion requires that revenue recognised reflects the value transferred to the customer. We recommend that the boards clarify that the entity should determine the reasons for the increase or decrease in prices to ensure the accounting reflects this principle. This could be accomplished by including the following guidance in paragraph 72:

If in a contract for repetitive goods or services an entity cannot demonstrate that the contracted amounts reflect an increase or decrease in value consistent with market pricing, an average pricing model might be more appropriate.

Contract costs

We agree with the decision to require capitalisation of costs that meet the definition of an asset. We support the boards' decision to include a practical expedient for contracts of less than one year but suggest that the boards clarify that the practical expedient should be applied consistently to contracts with similar characteristics and in similar circumstances.

We recommend that the boards clarify the meaning of 'anticipated contracts' and the impact of an anticipated contract on the amortisation period. For example, if a cost is capitalised because it will be recovered through performance on a single anticipated contract, we believe the entity should be able to extend the amortisation period as related contracts are signed if those contracts extend the period over which the entity derives economic benefits from those costs. We also suggest that the boards clarify that once an entity determines that a cost does not meet the capitalisation criteria, the cost cannot be capitalised at a later date even if better information becomes available about the entity's ability to recover the cost.

The boards should also consider whether the standard should refer to existing impairment guidance given the differences between IFRS and US GAAP in measuring impairments (for example, the extent to which the time value of money is taken into account). We also recommend the boards consider whether a converged approach to impairment should be applied to contract costs that are capitalised under the standard. The impact of time value of money on the measurement of a liability arising from an onerous performance obligation is also unclear.

Principal agent considerations

We acknowledge the boards' intent to provide guidance for determining whether an entity is acting as a principal or agent. We believe, however, that tension exists between paragraphs B17, B18 and B19. Paragraph B17 is derived from the transfer of control principle while the indicators in paragraph B18 are largely consistent with current guidance and are based on risks and rewards. Paragraph B19 also emphasises the obligation to fulfil over the other indicators in paragraph B18 and the principle in B17.

Consider an example of a travel agent that purchases an inventory of airline tickets. The travel agent has obtained control of the airline tickets and is exposed to the risk of loss if the tickets are not sold, is



able to set the price, and has credit risk. The travel agent appears to be the agent based on the guidance in B19 despite meeting several indicators in B18. We believe in this fact pattern the travel agent would be the principal under current guidance as it has exposure to significant risks and rewards. We recommend that the boards consider whether they intended to change current practice.

Transition

We appreciate the theoretical merit of retrospective application to increase consistency across periods presented. The cost and effort involved to implement this approach might, however, outweigh the benefits. We acknowledge the boards' efforts to reduce the challenges through practical expedients, but we believe opportunities exist to minimise the burden on preparers without significantly compromising the needs of users. We suggest that the standard allow entities to account for contracts prospectively if it is not practical to apply the standard retrospectively to those contracts.

We recommend the boards consider the implications of applying IAS 8, which requires disclosure of the impact of retrospective adoption on the current and prior year. We do not believe disclosure of the impact on the current year is useful for financial statement users and might be burdensome for preparers (for example, it could require running dual systems for a longer period of time).

We understand that implementing the new standard might be challenging for some industries and encourage the boards to continue to search for practical solutions that are consistent with the principles in the exposure draft. We recommend appropriate lead-time to enable entities that apply the standard retrospectively sufficient time to put in place the necessary systems to capture needed information.

We continue to support permitting early adoption for entities that today prepare their financial statements under US GAAP.



APPENDIX C – US GAAP CONSEQUENTIAL AMENDMENTS

Question 1: *Do you agree that the proposed amendments that codify the guidance in the proposed Update on revenue recognition have been codified correctly? If not, what alternative amendment(s) do you recommend and why?*

Notwithstanding our comments in Appendix A and Appendix B of this letter, we agree with the proposed amendments that codify the guidance in the proposed Update on revenue recognition.

Question 2: *Do you agree that the proposed consequential amendments that would result from the proposals in the proposed Update on revenue recognition have been appropriately reflected? If not, what alternative amendment(s) do you recommend and why?*

We generally agree that the proposed consequential amendments that would result from the proposed Update on revenue recognition are appropriately reflected. We agree with the proposed amendments that eliminate industry specific revenue recognition guidance but recommend the FASB consider whether certain superseded codification sections that describe the unique aspects of industry specific terminology and background should be retained as it might be helpful to preparers.