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Mr. Hans Hoogervorst
Chairman of the
International Accounting Standards
Board
30 Cannon Street

London EC4M 6XH
United Kingdom

Düsseldorf, 12 March 2012

Comment Letter of the German Construction Industry Association regarding IASB/FASB “Exposure Draft ED/2011/6 Revenue from Contracts with Customers (A revision of ED/2010/6 Revenue from Contracts with Customers)”

Dear Mr. Hoogervorst,

The German Construction Industry Association (Hauptverband der Deutschen Bauindustrie) welcomes the opportunity to comment on the proposals concerning revenue recognition rules included in the re-exposed draft (RevED) “Revenue from Contracts with Customers”.

We reviewed the proposals of the Board included in the RevED from the perspective of the German construction industry and against the background of experience collected to date with the standards currently in force. We precede our comments with some general remarks. These are followed by answers on the questions raised in the RevED.

I. General remarks

The remarks in this comment are based on our comments on the Discussion Paper (DP) from 17 June 2009 (1660-100 Comment Letter No. 40) and the Exposure Draft (ED) from 21 October 2010 (1820-100 Comment Letter No. 352).

The German Construction Industry Association is pleased that the IASB has included some of our remarks from the comment on the DP and the ED in the RevED, especially those regarding the clarifications on critical issues with respect to construction contracts, i.e. identification of separate performance obligations and performance obligations satisfied over time. We think that the proposals of the RevED are a significant improvement over the proposed guidance in the ED.

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However, the RevED still contains proposals that

- are not sufficiently clear,
- will result in information that is not decision useful and
- will cause high implementation and application costs.

a) **Contract modifications**

In our understanding of paragraph 19 the board plans to change the regulations regarding the point of time from which on contract changes have to be accounted for. The particular point of time for the consideration of a contract change the RevED refers to the date, the parties to a contract have approved a change in the scope of the contract, whereas the current regulation under IAS 11.13 refer to the fact that an acceptance of the contract change by all parties is probable. From this, we would like to ask the board on clarification on the following two aspects:

- Does the board really intend to increase requirements for the consideration of contract changes? If yes, what would be the benefit of such an increase compared to the current regulation?
- Is our understanding correct that the approval of the change by the parties in the scope of the contract as stated in paragraph 19 of the ED does not necessarily require the existence of a signed contract amendment? The wording of the ED could lead to the assumption that the rights from the change of the contract have to be legally enforceable. This would lead to a different accounting in different jurisdiction and would not comply with the substance over form-criterion in F.35 of the IFRS framework.

We are of the opinion that the effects of contract changes should be accounted for from the point of time the management regards an acceptance of the changes by all parties as probable and therefore includes it into the project calculation. Such a view would correspond to the management approach as referred to in IFRS 7 and IFRS 8 and would mean only minor deviations from the regulation currently in use.

b) **Identifying separate performance obligations: pattern of transfer**

The scope of the criterion "same pattern of transfer" proposed in paragraph 30 is **not sufficiently clear**. The effect of this criterion on unbundling might be quite different if the same period of time for the rendering of different services included in a multi-element contract is interpreted as a year or as a month.

c) **Performance obligations satisfied over time: right to payment criterion and relevance of customer acceptance**

The "Right to payment" criterion proposed in paragraph 35(b)(iii) might be **difficult to assess**, especially if the interpretation of the criterion depends on contract law which differs with the jurisdiction relevant for the contract. This would require a case by case assessment which is onerous and would infer with uniform accounting principles within an entity.

Furthermore, it is **not clear** if the indicator for transfer of control "customer acceptance" is a relevant factor for performance obligations satisfied over time. Looking at the placement of the passage relating to this indicator in the standard [paragraph 37(e)], it seems that it is not relevant for performance obligations satisfied over time. However, paragraphs B55-B58 do not explicitly address the irrelevance of "customer acceptance" for performance obligations satisfied over time.

d) Measuring progress towards complete satisfaction of a performance obligation: application of input-methods for contracts comprising significant components procured from another entity

The timing of revenue recognition for components constructed by suppliers / subcontractors that are part of an integrated performance obligation (paragraphs 46 and IE7) is **not clear**, i.e. recognition of revenue during construction or at delivery to customer.

e) Capitalisation of contract costs: scope of costs to fulfil a contract and Incremental costs of obtaining a contract

The scope of "costs to fulfil a contract" (paragraphs 91-93) is **not sufficiently specified** so that it is unclear what kind of costs should be capitalised (e.g. start-up costs relating to service contracts, mobilisation costs relating construction sites etc.).

Furthermore, we have difficulties to understand why the board does only include incremental cost as contract costs. This excludes most of the internal costs – except overtime costs – from being regarded as contract costs. In other standards (IAS 2, IAS 16 and especially IAS 38) refer to directly attributable costs and the asset definition. In our view, these criterions should also be used with regard to the capitalisation of contract cost, so that all costs directly attributable to the contract have to be capitalised, if they are likely to be refunded by the customer. Such a treatment would comply with the current regulation under IAS 11.21.

f) Disclosure requirements

An area of major concern are the proposed requirements for annual and interim financial reports which were largely carried over from the ED. As already stated in our comment letter to the ED, we believe that the proposed disclosure requirements will cause **unreasonably high costs**. With regard to the expected cost-benefit-relation, we believe that the proposal will **not improve decision making**.

The proposed disclosure requirements are substantially more extensive and detailed than the existing requirements. The inclusion of the detailed qualitative disclosure requirements will likely increase the size of disclosures. These additional disclosures will likely not translate into more decision useful information for the users of financial statements. Instead, we continue to believe that the current disclosure requirements in IAS 11, IAS 18 and IFRS 8 are appropriately addressing the information needs of investors without overburdening them with disclosure overload.

To improve prospective information on revenues, other indicators that are already used in management and capital market reporting such as orders on hand could be included in disclosures.

g) Effective date and transition

Implementation on 1 January 2015 is **difficult and onerous**, because of the necessary changes to policies, systems, and procedures, especially due to the proposed disclosure requirements. A delay in the publication of final standard will aggravate this problem. We urge that there should be a minimum period of two years between the date of issuance and the effective date due to the many adjustments to reporting systems and processes that are necessary in order to comply with the proposed standard on revenue recognition.

Also, retrospective application to running long-term contracts is **onerous**. We perceive a serious mismatch between the benefit of retrospective application for information provided to decision-makers and the costs to produce the required data.

II. Answers to the questions in the revised Exposure Draft

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 recognizes 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?

In general, we agree with the proposals for revenue being recognised over time. However, proposals central to revenue recognition in construction contracts are not sufficiently specified.

We think that further clarification is required regarding the following issues:

The “**right to payment**” criterion proposed in paragraph 35(b)(iii) might be difficult to assess, especially if the interpretation of the criterion depends on contract law which differs with the jurisdiction relevant for the contract. This would require a case by case assessment which is onerous and would infer with uniform accounting principles within an entity.

Furthermore, it is not clear if the indicator for transfer of control “**customer acceptance**” is a relevant factor for performance obligations satisfied over time. Looking at the placement of the passage relating to this indicator in the standard [paragraph 37(e)], it seems that it is not relevant for performance obligations satisfied over time. However, paragraphs B55-B58 do not explicitly address the irrelevance of “customer acceptance” for performance obligations satisfied over time.

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 that credit risk should not be included in the measurement of revenue. However, we do not think that the proposed presentation provides decision-useful information. For one, the proposed presentation is a significant change from the current practice of presentation of credit risk. Also, we think that the disclosure requirements of IFRS 7 already provide sufficient information on credit risk that is also superior to the proposed requirements.

Regarding the collectability criterion in paragraph 69 we ask the board for clarification on the fact whether or not the presentation of an impairment on receivables or change in the measurement of an impairment in profit or loss as a separate line item adjacent to the revenue line item really depends on the existence of a significant financing component in accordance with paragraph 58. If this is the intention of the board, we ask for further clarification on the reason why the impairment (or loss) has to be shown as a deduction from revenue at the date of recognition, regardless of the existence of a financing component. We are of the opinion that initial and subsequent measurement of the credit risk should not be disclosed separately. If the receivable contains a material financing component, we do not regard a deduction from revenue as an appropriate treatment.

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 refrain from answering this question.

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 regret that the RevED has not adopted the treatment tentatively proposed in the deliberations of the ED. As stated in our comment letter to the ED, we do not think that onerous test should be performed at the separate performance obligation level but on the contract level as required by IAS 37. The recognition of a liability for a separate performance obligation will result in information that is not decision-useful if the overall contract is profitable.

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.

No, we do not agree that an entity should be required to provide each of those disclosures in its interim financial reports. The proposed disclosure requirements are substantially more extensive and detailed than the existing requirements. This also applies to the disclosure proposed for annual financial reports.

As already stated in our comment letter to the ED, we believe that the proposed disclosure requirements will cause **unreasonably high costs**. With regard to the expected cost-benefit-relation, we believe that the proposal will not improve decision making. The proposed disclosure requirements are substantially more extensive and detailed than the existing requirements. The inclusion of the detailed qualitative disclosure requirements will likely increase the size of disclosures. These additional disclosures will likely not translate into more decision useful information for the users of financial statements. Instead, we continue to believe that the current disclosure requirements in IAS 11, IAS 18 and IFRS 8 are appropriately addressing the information needs of investors without overburdening them with disclosure overload. To improve prospective information on revenues, other indicators that are already used in management and capital market reporting such as orders on hand could be included in disclosures.

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?

We agree.

We would be pleased to answer any questions that you might have or discuss any aspect of this letter.

Yours sincerely

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