Exposure Draft ED/2010/06 “Revenue from Contracts with Customers”

Dear Madam and Sir,

We appreciate the opportunity to respond to the ED “Revenue from Contracts with Customers” jointly developed by the IASB and the FASB.

Over the last two years, France Telecom and other telecommunications companies have been engaged in extensive discussions with the IASB Staff and Board members regarding the impact on the telecommunications industry of both the Discussion Paper, ‘Preliminary Views on Revenue Recognition in Contracts with Customers’ (the ‘DP’) and the Exposure Draft “Revenue from Contracts with Customers” (the “ED”). We would like to thank you for these exchanges.

The discussions covered the industry’s business models, the concerns expressed by our users on the Board’s proposals, and the significant operational challenges that would arise if they were to be implemented. We also proposed amendments to the draft ED.

In order not to be repetitive with information already presented, this letter should be read in conjunction with our letter dated June 18, 2009, our joint letters with Telefonica, Deutsche Telekom, Telecom Italia and Vodafone dated January 26, 2010 and April 20, 2010, the presentations made by ourselves or our peers during the outreach activities of Board members and the Staff.
The users views we refer to in this letter are derived from the Financial Dynamics report appended to our comment letter on the DP, from the discussions held in April 2010 between members of the Boards and two industry’s analysts and from other private exchanges between investors and our investors’ relations department.

While many comments raised in this letter are shared by other companies in our industry, we do have specific views. Hence, this letter represents solely the views of France Telecom.

In brief

We are disappointed that the ED published takes into consideration neither the specificities of business models nor the concerns highlighted by the telecommunications industry and its investors.

The proposed standard maintains the rejection of specific treatments for the upfront subsidy granted to the customer and for the nature of telecommunications contracts (high volume of contracts, frequent modifications, variability of components, delivery through time, etc.). It thus retains the proportionate fair value revenue allocation taking into account for contracts with a commitment from the customer, expected revenues which recovery is both legally contingent on the delivery of communications services not yet rendered and highly dependent on the volatile behaviour of the customer.

In these conditions, we strongly reaffirm that as it stands the ED neither improves financial reporting nor meets the costs/benefits criteria for a final standard:

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The Exposure Draft

1. will **not reflect business** and marketing practices in a relevant manner
2. **will reduce comparability** of reported revenues in the industry by introducing areas of judgment for estimates, likely discrepancies in application of the ED, unjustified differences in revenue reporting between distribution channels and between customer retention models.
3. **will decrease decision-making usefulness** of the reported revenue for investors, analysts and other users; in fact, users informed us they will restate revenues back to current practice in order to eliminate management estimates, discrepancies in revenue reporting between distribution channels or customer retention models, and decorrelation with actual cash flows.

The current IAS18

1. results in accounting that **mirrors the underlying nature of the business** as viewed by investors, analysts and other users of the accounts, i.e.
   - that customer acquisition costs in the form of equipment discounts are typically incurred up-front to secure future service revenue; and
   - that period commitment included in some contracts are simply a tool among others to increase customers loyalty;
2. provides users with **good comparability** across markets for the industry and has enabled revenue accounting to be substantially **convergent across the world**.
3. results for users in **reliable revenue information** despite large customer numbers and near-infinite contract variability;
4. is perceived by users as **not unduly sensitive** to management estimation;
5. results in recognised revenue that **correlates closely to the cash flows** generated from customers, a key attribute to users; and
6. provides to users **strong predictive**
There is a real risk that the industry will be unable to operationalize the proposed standard. Coping with the volume of contracts and of components & modifications of each contract renders the feasibility and timeframe of systems changes not only excessively costly but highly uncertain if not unlikely.

Thus, we entirely disagree with the Boards’ statement in BC 244 about its analysis of costs and benefits but are encouraged by the Boards’ statement in BC 246 that it will continue to consult widely about modifications to reduce the burden without impairing reliability.

Appendices B and C present an update of our initial comments on the DP in light of the ED and our answers to the questions for respondents.

Our proposals to solve the deadlock

As requested by the Boards, we have tried to identify new proposals to overcome the current deadlock.

1. Reconsider the distinction between marketing incentives and revenue generating activities
2. Introduce a “lower of contractually stated price and relative fair value allocated price” for the satisfied performance obligation.
3. Reinstate the contingent revenue cap.
4. Clarify §38 and foll. to include situations such as those encountered by the industry where the lack of availability of data and systems does not enable an entity to identify the possible consideration amounts and probabilities per contract necessary to comply with the standard./ where the dispersion between the possible and actual outcomes per contract is too wide.

These proposals are developed in Appendix A.

Conclusion

We believe the ED as it is should not be issued as a final standard. The existing revenue recognition mechanisms have proved to work well and provide decision-useful information to users of financial statements by reflecting appropriately the economics of transactions and the performance of entities.

Naturally, we remain open to further discuss our proposals to overcome the current deadlock.

We hope you find these comments and proposals useful and would be pleased to provide any further information you might require.
Yours sincerely

s/ Gervais Pellissier
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Deputy Chief Executive Officer,
Group Finance and Information systems

s/ Stéphane Pallez
Stéphane Pallez
Deputy Chief Financial Officer

s/ Xavier Pichon
Xavier Pichon
Head of Investors Relations

s/ Valérie Théond
Valérie Théond
Chief Accounting Officer

s/ Nicolas de Paillerets
Nicolas de Paillerets
Director of Group Accounting Principles

Cc:
Mr. Jean-Pierre Jouyet, AMF
Mr. James L. Kroeker, SEC
Mrs. Françoise Flores, EFRAG
Mr. Jérôme Haas, ANC
Appendix A- Dealing with the most significant sources of issues for telcos

The most significant sources of issues set forth in our cover letter are:
- the proposed reallocation of ongoing service revenue to the equipment we provide with a discount to customers to allow them to access our services, and
- the constant modifications of contracts.

The reallocated revenue would be recognised upfront, in advance of billings, and would lead to a contract asset.
- This contract asset is not legally enforceable if we, as operators, do not fulfil our contractual obligations to provide future services to the customer.
- It will not necessarily be recoverable without significant costs if the customer breaks its period commitment.
- It would be highly dependent on estimates of the actual vs. contractual commitment period, and
- it leads to cumulative catch-up adjustments if modifications are determined to be price interdependent with the initial contract.

We note that the Boards have contemplated other methods apt to be relevant for our industry:

The residual method is discussed in BC122-124 and is viewed unnecessary if an entity is required to estimate stand-alone selling prices. However, we understand the Board could reconsider it for the reasons expressed in BC123 (less complex, less costly). We do not retain it as a viable alternative for the following reasons:
- The residual method provide only a limited relief to telcos: its implementation will remain difficult because of the complexity of the tariff structure for the telecom services.
- It will not achieve the same level of comparability as today because revenue would no longer be independent from distribution channels and marketing environment.
- It will also require the acceptance by the Boards of a significantly downgraded implementation of the accounting model as the data and systems will not be in place to deal with the asset/liability reporting and the disclosures.
- Furthermore, significant testing would be necessary before confirming the effectiveness and reliability of the approach.

The reverse residual method that the Boards consider as appropriate when there is a directly observable price for one of the obligation but not the other, does not seem applicable.

After a careful consideration, we see no other way to overcome the current deadlock than keeping the current accounting output within the frame of the ED. As such, it should eliminate
- the ED inconsistency in the way revenue will be reported when the subsidy is directly channelled to a customer that signs up in the operator outlets or indirectly channelled to a customer by a third party distributor who provides the handset and signs up the customer for the services of the operator;
- the ED discrepancy in the way telecommunications revenue will be reported between contracts with or without commitment from the customer, which does not portray the continuum of the various marketing approach to fostering loyalty.

**Proposal 1. Reconsider the distinction between marketing incentives and revenue generating activities**

BC43-44 delineates “marketing incentives as being incurred independently of the contract they are designed to secure” and states that “even if a conceptual justification could be found to distinguish goods or services that are marketing incentives from those that give rise to performance obligations, it would be difficult to develop criteria to make that distinction in practice”.

We have already suggested that the Board could choose to characterize the initial subsidy as a marketing incentive to be recognized against the contract consideration at the time of granting.

We do not believe it is so difficult to develop indicators:
- It is granted in order to sign up a customer and are managed as costs of obtaining a contract,
- The subsidy applies on goods or services that are not mainstream,
- The subsidy would be characterized as a direct payment or the delivery of a product at a price substantially lower than its cost to the entity.

Alternatively it could be characterized as a promise within the contract that is delivered upfront as we had proposed during the Paris meeting in February 2010.

Both characterizations would be consistent with the Board’s view on expensing the costs to obtain a contract and with the contract consideration approach. This approach
- preserves the key attributes of the ED,
- will satisfy many users for the very reasons summarized in the costs/benefits analysis of the ED vs. IAS18,
- safeguards the benefit of the relative fair value allocation for the discounts that are granted on the undelivered performance obligations (subject to our comment in relation to IFRIC13),
- is coherent with the contractual and legal structure and reflects the acceptance by the entity of the risk of non performance of the customer.

**Proposal 2. Introduce a “lower of contractually stated price and relative fair value allocated price” for the satisfied performance obligation**

Replacing the stand alone selling prices fair value allocation by a “lower of contractually stated price and relative fair value allocated price” for the satisfied performance obligation would result in a similar accounting as today. It is nothing more than adjusting the rule based allocation of contract consideration proposed by the Boards.

Although we are aware of the Boards views expressed in BC127 and 129, we encourage the Boards to reconsider their views for the same reasons as the ones described here above in proposal 1.
Proposal 3. Reinstate the existing contingent revenue cap

The current accounting model used by the major telecommunications services operators within Europe, the United States and Japan is the relative fair value model, with a ‘contingent revenue cap’ applied to up-front equipment provided as a contract incentive to the customer. Equipment revenue is typically the net price paid up-front by the customer; service revenue is dependent upon the provision of services and on customer purchase decisions and is recognised as services are delivered.

We are aware of the reasons developed by the Boards in BC95 to reject this approach for conceptual reasons.

Nevertheless it does not imply that the Boards should not reconsider its position, at least because of the preference expressed by many users for such an approach. It also preserves most of the characteristics of the ED.

We note that reinstating a contingent revenue cap would probably not affect long term contracts accounting as a transfer of control implies that the recognized revenue is not contingent on the satisfaction of future performance obligations.

Proposal 4. Clarify §38 to include situations such as those encountered by the industry

In addition to the previous proposals, there is one other approach: a clarification that the exceptions described in §38 and following can apply to the fact pattern of the industry. Although not explicitly, the limitation to estimates in §38 is probably what led the Boards to the conclusion that, for our industry, only the minimum consideration linked to the period commitment should be included in the allocation.

As explained, this conclusion obviates that contract modifications, upgrading/downgrading the services or monthly consideration, extending/shortening the period for which the customer is committed, are frequent throughout the original period commitment. So the move would be to clarify the acceptability for the Boards of an extended limitation.

In fact, we believe the indicators in §39 (a) “the consideration amount is highly susceptible to external factors” and (d) “the contract has a large number of potential consideration amounts” are particularly appropriate to the industry and should not be read as imposing to take as consideration the contractually committed amount, contrarily to the current views expressed by the Board (e.g. the Investor Perspective “Revenue recognition and your mobile phone” published by the IASB).

We also note the use by the Boards of the term “variable consideration” in the limited context of the customer promising a variable amount of consideration could contradict our view. We believe the variability of the contract consideration (excluding collectibility) derives also from de facto variability in the contract term, scope or pricing, either on the initiative of the customer or of the supplier or of its distributors in response to various external factors (competition, technological evolution, regulation etc.).

In brief, the motivations for the requested clarification are:

- the influences of competition and of technology evolution on the behavior of customers and on the offers of the entity (contract modifications) reduce the relevance of past experience.
- the dispersion between the possible and actual outcomes per individual contract is too wide to enable an adequate accounting per contract even though one has experience with similar
contracts; i.e. users would find it more useful if the entity recognises revenue only when the entity is resolved;

We also believe that the lack of availability of data and systems which does not allow an entity to identify the possible consideration amounts and probabilities per contract necessary to comply with the standard should be included in the clarification. This in fact would be very similar to the mention in IAS11 that it is necessary for an entity to have an effective internal financial budgeting and reporting system in order to produce reliable revenue and costs estimates (IAS11.29).

If the principle of a clarification is accepted, the existing mentions of the telecommunications services in the application guidance and in the BC’s should be eliminated together with a clarification of the Basis for Conclusions and in the Standard: for example [deletion addition]:

Basis for conclusions

“Constraining revenue recognition when consideration is variable/uncertain

BC 90 The Boards considered whether to constrain revenue recognition if the customer promises a variable consideration the amount of contract consideration or transaction price is variable either contractually or de facto. The Boards decided to constrain the contract consideration and transaction price because revenue is an important measure to users of financial statements when valuing an entity and because a significant portion of errors in financial statements have related to the overstatement or premature recognition of revenue.

BC 91 […]

BC 92 For an entity to identify possible amounts and reasonable estimate their probabilities, the boards concluded that the entity would need experience (either its own or the experience of others) with similar types of contracts and customers showing a limited dispersion of contract considerations and transactions prices. Without that experience, the level of uncertainty or variability in the estimate of the variable consideration would be too high for users to find useful the measurement of any revenue recognised on the basis of that estimate. In other words, a user might find it more useful if an entity recognises revenue only when that uncertainty is resolved.

BC 93: The Boards decided that experience was necessary but not sufficient to estimate variable consideration reasonably. The entity’s experience must also be relevant to the contract because the entity does not expect significant changes in circumstances (i.e. the circumstances surrounding the current contract are expected to be similar to those surrounding the similar contracts in the past). To help an entity assess whether its experience is relevant to the contract, the Boards decided to specify factors that would reduce the relevance of that experience. Those conditions were derived in part from existing guidance in US GAAP on estimating sales returns.

BC93bis The Boards also recognized the necessity of the availability of data and systems to allow an entity to identify the possible consideration amounts and probabilities per contract necessary to comply with the standard. They noted that in some industries (e.g. telecommunications) such availability may not be present because of the way the entities operate their business.
Standard

*Determining the transaction price*

38 An entity shall recognize revenue from satisfying a performance obligation only if the transaction price can be reasonably estimated. The transaction price can be reasonably estimated only if *both* all the following conditions are met: (a) the entity has experience with similar types of contracts (or access to the experience of other entities if it has no experience of its own); and (b) the entity's experience is relevant to the contract because the entity does not expect significant changes in circumstances; and (c) the entity has the appropriate data and systems in order to make the estimates and accounting required by the standard.

39 Factors that reduce the relevance of an entity's experience include the following: (a) the consideration amount is susceptible to external factors (for example, volatility in the market, judgment of third parties and risk of obsolescence of the promised good or service, competitors behaviour, regulatory interventions, customers requests, etc.) or internal factors in response to those (for example, practices with or without effect on the contract consideration like upgrading or downgrading the goods or services, extending or shortening a period commitment, etc.); (b) the uncertainty about the amount of consideration is not expected to be resolved for a long time; (c) the entity's experience with similar types of contracts is limited; and (d) the contract has a large number of possible consideration amounts.
Appendix B- Update on our first comment letter

Our first comment letter included a report by Financial Dynamics of the feedbacks of leading industry analysts. These initial views were reaffirmed in the meeting of the Boards with analysts in April 2010 and during private exchanges between investors and our investors’ relation department. It also included a detailed description of the IT systems in which a telecommunication company operates and the potential impact of the DP.

In summary, our first letter suggested the Boards reconsider their search for a single model, develop additional guidance on IAS11 and IAS18 where necessary, and take the necessary time to make a thorough analysis of the desirable attributes of revenue for users. More specifically,

A. It encouraged the Boards to thoroughly analyze three areas that have fundamental consequences on how to develop a new model for revenue recognition:

   o The Boards should define what revenue should portray in the income statement, and the desirable attributes of revenue for its decision-usefulness to users;
   o The Boards should build in at an early stage of their standard setting an assessment of the risk of altering the control environment of financial reporting;
   o Similarly, the Boards should embed earlier into their developing process an evaluation of the possible accounting processes changes.

At this stage, we believe (a) our requests remain fully valid and are consistent with comments by Actéo, EFRAG or ANC, and (b) the Boards have not demonstrated the new standard would improve financial reporting under IFRS at a reasonable cost as stated in BC 239-247.

B. The letter also focused on five fundamental areas with respect to the proposed revenue recognition model:

   o The contemplated boundaries of a contract raise significant concerns for the telecommunications industry: we strongly encourage the Boards to assess the positive benefits associated with not accounting for options that are difficult to value.

   In our meetings, the Boards clarified it does not expect the industry to consider at the initiation of a contract consideration for which there is no firm commitment from the customers: e.g. prepaid contracts are limited to the initial delivery of the handset and the nominal communications, post-paid contracts where the customers commits itself for a certain period do not include options for additional services (out of bundle services: add-ons, additional call minutes or data transfer; renewals).

   We note the reasoning expressed in BC81-83 when defining the transaction price could be read as contrary to the Board’s clarification.

   Similarly, however helpful the illustration in B26, we fear some will challenge on its basis the Board’s clarification or read the notion of ‘within the range of prices typically charged’ as requiring the demonstration of such an assessment.
We respectfully suggest that the notion of “parties are committed to satisfying their respective obligation” or “the entity... can identify each party’s enforceable rights” be clarified so as to mean performance obligations and right to consideration are established (price, quantity and nature of goods or services), and exclude options.

We also would like to point out that the capacities of telcos to account for a contract modification would rest upon the qualification of the modification as not price interdependent. We are concerned about how this notion will be interpreted and believe also that accounting for a modification as cumulative change will not always best reflect the economics for the modification while at the same time increase significantly the cost of compliance.

- The proposed definitions of a customer and of a performance obligation do not enable to segregate sales incentives from other performance obligations and affect comparability.

BC43-44 delineates “marketing incentives as being incurred independently of the contract they are designed to secure” and states that “even if a conceptual justification could be found to distinguish goods or services that are marketing incentives from those that give rise to performance obligations, it would be difficult to develop criteria to make that distinction in practice”.

We have already suggested that the Board could choose to view the initial subsidy as a marketing incentive and require recognizing it against the standalone selling price of the first delivered item. This would have been consistent with the Board’s view on expensing the cost to obtain a contract. It would also have eliminated the inconsistency in the way revenue is reported when the subsidy is directly channelled to the customer that signs up in the operator outlets or indirectly but in substance channelled to the customer by another party (a third party distributor) that provides the handset.

We therefore respectfully suggest the Boards review their preliminary assessment of the subject.

- We encourage the Boards to consider constraining revenue to consideration that is certain by evaluating the advantages of such an approach, especially in terms of confidence in reported figures

We fully disagree with the reasoning expressed in BC82 for defining the transaction price and in BC90 and foll. for constraining revenue recognition when consideration is variable.

We note that users are extremely sensitive to the high degree of certainty attached to the current revenue recognition model that is not unduly sensitive to management estimation.

We respectfully suggest to the Boards to investigate more fully both the users’ views on the adequacy to their needs of estimates in revenue reporting and the preparers’ views on the impact of estimates on internal controls and accounting processes.

The rejection in BC95 of the contingent revenue cap is specifically discussed in Appendix A together with the residual method that was rejected by the Boards (BC122 and foll.).

- Beyond our industry, the notion of transfer of control as defined is not fully operative and does not provide the expected decision usefulness to users
In fact, our industry is confronted to the lack of clarity of the notion of transfer of control for those equipments that have no actual stand-alone value for the customer except for accessing some of our services. A similar difficulty arises within the context of the Exposure Draft “Leases”.

The notion of “distinct goods or services” could be helpful: in BC49 the Boards explain how to overcome the difficulty attached to the notion. However it does so by limiting the requirement a promised good or service to have a distinct function and a distinct profit margin to situations where the goods or service is not sold separately and with considerations attached to the notion that nullify the potential usefulness of the notion almost completely.

We respectfully suggest that the difficulties the Boards face can only be alleviated by recognizing the role in the standard of business models as the example of the contract management illustrates it.

- In our industry the pervasive constraint of cost to preparers can not be met with the proposed asset/liability accounting model

In the summary of comment letters on the DP, the Boards recognized some of those concerns: “§12. Apart from those industries noted above that were unsure about how the model be applied, three industries raised particular concerns about the proposed model: a) long term construction, b) telecommunications, c) insurance. §14. All respondents from the telecommunications industry have concerns about the costs of implementing the proposed model.”

No satisfactory answer has been included yet in the ED in that respect and would like to point first that costs to preparers are ultimately costs to the shareholders, and second that we have provided evidence that there are also other significant costs to users.
Appendix C- Questions for respondents

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

We agree that it is important to set out a principle as to when it is appropriate to combine two or more contracts and account for them as a single contract.

Nevertheless we are concerned that a requirement to combine all contracts that are price interdependent may be unnecessarily complex in practice, notably with respect to contract modifications and loyalty programs.

In that respect, paragraph 14, ‘the price of a contract is not interdependent with the price of another contract solely because the customer receives a discount on goods or services in the contract as a result of an existing customer relationship arising from previous contracts’ is a right step forward.

Example 2 illustrates the difficulty of the notion as the reasoning behind the conclusion and its compatibility with the various paragraphs of the standard is unclear.

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 this principle? If not, what principle would you specify for identifying separate performance obligations and why?

We support the notion of distinct good or service for separating performance obligations but disagree with how a distinct good or service is defined.

In considering whether a promised good or service is distinct, we believe that only an entity’s own customary business practices should be considered, rather than the business practices of any other entities as many different business models exist.
In addition, in § 23 only “distinct goods or services” not sold separately need to have a distinct function and a distinct profit margin with considerations attached to the notion that nullify the potential usefulness of the notion almost completely.

**Question 3 — Do you think that the proposed guidance in paragraphs 25–30 and related application guidance is 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?**

First of all, we believe that the definition of control as proposed in this ED is not consistent with other standards like IAS 27 making it more difficult to understand the characteristics of the proposed definition. In fact we believe that the transfer of control overlay to achieve the objective of a single standard for construction contracts and sale of goods or services masks the fact that in construction contracts there is often a degree of shared control over the asset under construction. Similar situations exist for licenses or services and goods.

With respect to our industry, the indicators of transfer of control are not very clear for those equipments that have no actual stand-alone value for the customer except for accessing some of our services. A similar difficulty arises within the context of the Exposure Draft “Leases”.

**Measurement of revenue**

**Question 4 — The boards propose that if the amount of consideration is variable, an entity should recognize revenue from satisfying a performance obligation only if the transaction price can be reasonable 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 recognize revenue on the basis of an estimated transaction price? If so, do you agree with the criteria in paragraph 38? If not, what approach do you suggest for recognizing revenue when the transaction price is variable and why?**

We believe constraining revenue when it is not highly probable is an absolute necessity and believe the current wording suffers from different possible interpretations, esp. because of the basis for conclusions.

The criteria in § 38 should be expanded to include situations where the data and systems/processes to make the required estimates are not present or can not be designed.

We also disagree with probability weighted amount of consideration and note that the notion of variable consideration is unclear.

Together with remarks on the indicators, we further discuss these matters in Appendix A Proposal 4.
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 recognizes when it satisfies a performance obligation rather than whether the entity recognizes revenue? If not, why?

We do not think that a customer’s credit risk should be reflected in revenue because:
- it results in an excessive sophistication of accounting,
- a commercial or industrial company business model is not to originate and sell a receivable with a high level of credit risk.

We also note that a customer might be unwilling to pay for reasons other than its credit-unworthiness and that the ED is somehow confusing about the distinction between credit-worthiness and other causes of non-performance that can result in the non collectibility of initially agreed payments.

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?

In principle, one could agree. However we have strong reservations in the way the ED deals with the subject: we believe that if applied
- any computation should be done on receivables (between billing and collection) and prepayments; computation on the differential between the relative fair value allocation amounts and the contractual amounts will lead to significant complexities (as is the case with the Boards proposition for the telecom industry);
- the § 44 should explicit what is a material financing component, clarifying that it is appreciated at the level of an individual contract and relates to a satisfied performance obligation; a relief of 12 months could also prove pragmatic;
- the basis for conclusion should better explain and indicate that an advance payment in relation to a sale contract should be accounted differently from the requirements of IAS39.

We also suggest that a guidance be provided for situations where multiple performance obligations are delivered over time.

Question 7 — Paragraph 50 proposes that an entity should allocate the transaction price to all separate performance obligations in a contract in proportion to the stand-alone selling price (estimated if necessary) of the good or service underlying each of those performance obligations.

Do you agree? If not, when and why would that approach not be appropriate and how should the transaction price be allocated in such cases?
We believe the proposed approach is rule based, negates the various business models that may exist and lead to clear inconsistencies as is illustrated by the onerous obligation in a globally profitable contract.

We also believe that, after the initial allocation, changes in the estimated transaction price should be allocated to different performance obligations based on the relevant facts and circumstances.

**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 recognize an asset only if those costs meet specified criteria.

Do you think that the proposed requirements on accounting for the costs of fulfilling a contract are operational and sufficient? If not, why?

We agree with the proposals and believe they are reasonably operational.

**Question 9** — Paragraph 58 proposes the costs that relate directly to a contract for the purpose of (a) recognizing an asset for resources that the entity would use to satisfy performance obligations in a contract and (b) any additional liability recognized for an onerous performance obligation.

Do you agree with the costs specified? If not, what costs would you include and why?

We agree with the costs specified for (a) as the full direct cost method (i.e., including in the cost of an asset both incremental and allocated costs that relate directly to the asset),

We agree with the non capitalization of the acquisition costs of a contract, we note that if a contrary decision was taken the cost eligible should ensure that the costs capitalization when using an indirect channel or a direct channel should be similar (i.e. the incremental notion may be inappropriate).

We disagree with an initial allocation of the price leading to an onerous performance obligation on an otherwise profitable contract. Assuming the question relates to an onerous contract, we agree with the cost trigger and the scope of costs chosen by the Boards but disagree with the probability weighted measurement basis. This is consistent with our rejection of that basis for the transaction price.

**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?
We agree with the disclosure of the significant judgments (§ 81-83) if any and of the nature of the performance obligations (§77).

For the other qualitative and quantitative disclosure, we disagree
- with the proposed mechanical reconciliation of contract balances, as we believe the disclosures in the statement of cash flows or of the relevant captions of the statement of financial positions should suffice.
- with the disclosure of any liability for onerous performance obligation (or contract): we believe a disclosure is pertinent only if a significant contract ‘derails’.

Please refer also to Question 12 for the disaggregation of revenue.

Question 11 — The Boards propose that an entity should disclose the amount of its remaining performance obligations and the expected timing of their satisfaction for contracts with an original duration expected to exceed one year.

Do you agree with that proposed disclosure requirement? If not, what, if any, information do you think an entity should disclose about its remaining performance obligations?

We disagree with disclosing the gross amount of performance obligations at balance sheet date, as this negates the initial reasons given for the net presentation. Only in those situations where the business of the entity is dependent on a limited number of high value contracts may this information be useful. In other circumstances, a simple explanation of the types of contract should suffice.

We also disagree with the timing disclosure and most of the reasons expressed in BC 179 ((a), (c), (d), and (e)). We think it is less pertinent than information about the degree of contracts concentration in the amount of Performance Obligations (“POs”). We remain uncertain about how points (a) and (b) (executory contracts) in BC177 are addressed in the gross presentation of POs.

Question 12 — Do you agree that an entity should disaggregate revenue into the categories that best depict how the amount, timing, and uncertainty of revenue and cash flows are affected by economic factors? If not, why?

We believe that the requirements of IFRS8 should be sufficient to encourage the appropriate disaggregation.

Stating the main economic drivers that affect the reported revenue is also more a subject of management commentary. We nevertheless understand the need:
- for a minimal depiction of the business models and
- for quantifying the effect on reported revenue of changes from one period to another of exchange rates or consolidation perimeter.

We note the standard itself may introduce uncertainty in reported revenue and increase the discrepancy between the reported revenue and cash flows, both outcomes that we do not believe to be desirable in terms of quality of financial reporting.
Effective date and transition

Question 13 — Do you agree that an entity should apply the proposed requirements retrospectively (that is, as if the entity applied the proposed requirements to all contracts in existence at the effective date and in the comparative period)? If not, why?

Is there an alternative transition method that would preserve trend information about revenue but at a lower cost to preparers? If so, please explain the alternative and why you think it is better.

Realistically there is little doubt that users will require retrospective information, and that they will wish this retrospective information be not limited to one comparative year.

The real issue then is the feasibility of a retrospective remeasurement: that feasibility will be significantly lessened and probably up to the point of non-feasibility if the proposed model diverges significantly from the current one and if the entity has a significant volume of low value, different contracts as it is unlikely that a dual recording can be achieved or that the data model and systems can be redesigned.

This question in fact raises the question of the costs/benefits of the proposed standard.

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

We think application guidance is helpful only if the principles are clear and the examples are well articulated with the principles. In the answers to other questions, we illustrate that it is not always the case and suggest some area where guidance is necessary.

We also have a similar concern of articulation of the basis of conclusions with the standard.

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?

We understand the Boards distinction and believe the guidance is reasonable in that respect, even if we recognize that it may be difficult to address the distinction when the customer is covered by a statutory and an additional contractual warranty.

However we remain unconvinced about the ‘failed sale’ approach for the latent defect warranties and believe the current cost model has not proved inadequate.

Question 16 — The boards propose the following if a license is not considered to be a sale of intellectual property:

(a) if an entity grants a customer an exclusive license 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 license; and

(b) if an entity grants a customer a non-exclusive license to use its intellectual property, it has a performance obligation to transfer the license and satisfies that obligation when the customer is able to use and benefit from the license.

Do you agree that the pattern of revenue recognition should depend on whether the license is exclusive? Do you agree with the patterns of revenue recognition proposed by the boards? Why or why not?

Generally a license is a right of use, not a sale of Intellectual Property (IP). So we are confused by the examples of the payroll processing software in BC225 to explain that it is a characteristic of a non exclusive license that the asset obtained by the customer is something else than the transfer of control of intellectual property, when in BC223 this seems to be also the characteristics of the exclusive licenses.

We suspect the distinction between exclusive and non-exclusive licenses made by the Boards is a kind of proxy to achieve the intended results of a continuous performance by the grantor for the exclusive license and of a simple sale on delivery for mass-selling of licenses. We do not think the notion of exclusivity is very robust in order to assess the constraint imposed on the grantor.

If licenses are rights of use, it would be better addressed in the ED leases (which could be renamed rights of use) although we are aware the Boards decided to scope out intangibles from that ED.

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?
We agree that it is necessary to address those sales of assets and that there is no reason why the principles should differ from the sales of goods and services that are an output of an entity's ordinary activities.

**Additional matters:**

**Asset / Liability accounting**

B91 explaining §64-68 makes it clear that the accounting required by the standard is the separate accounting of contract assets and liabilities and their netting for their presentation in the statement of financial position. We had already called the attention of the Boards on the consequences of the asset / liability concept they develop for the accounting systems and processes. Such an approach increases the cost of compliance significantly.

**Principal vs. agent considerations**

We believe the proposed guidance does not take into account the development of situations where two parties share an economic risk by entering into a revenue sharing arrangement and even limits the previous understanding by the emphasis over control in the ED. It does not address either dual relationship with a customer where a supplier compensates costs incurred by another supplier. In fact the guidance rests upon historical fact patterns that do not keep pace with the new ecosystems.