Exposure Draft ED/2011/6: Revenue from Contracts with Customers

Dear Sir/Madam,

Thank you for the opportunity to comment on your Exposure Draft ED/2011/6 Revenue from Contracts with Customers. The Volkswagen Group is one of the world’s leading automobile manufacturers and the biggest carmaker in Europe. The group currently operates 94 production plants in Europe, the Americas, Asia and Africa. Around the world, more than 500,000 employees produce more than 34,000 vehicles or are involved in vehicle-related services each working day. The Volkswagen Group sells its vehicles in more than 150 countries. With our 100%-owned subsidiary Volkswagen Financial Services AG we are also the largest automobile financial services provider in Europe. On behalf of Volkswagen AG, Wolfsburg, we are pleased to provide you with the requested remarks to the proposed Re-Exposure Draft in response to your invitation to comment.

Many of the proposals made in this Re-Exposure Draft contain improvements to the ED/2010/6. However, we are still unconvinced that a new Standard is necessary. In our view, so far there are only a few or minor regulatory gaps in the current standards. A complete revision and especially a retrospective application of the new standard lead to an unnecessary work load. The adjustment of IAS 11 and IAS 18 regarding the regulatory gaps is from our point of view sufficient.

Nevertheless, we present the following key statements:
We appreciate the distinction between revenue recognition over time and at a point in time. Partially, we see problems concerning the interpretation of the criterion „alternative use“. From our perspective certain issues such as the collection of license fees lead to questions regarding the interpretation.

- Impairment losses should not be shown straight under revenues.
- The assessment of whether an onerous obligation exists, should take place on contract level rather than on performance obligation level. Furthermore, the assessment should be restricted to contracts with revenue recognition over time.
- A retrospective application of the new standard should be quit since it would lead to substantial efforts. This substantial effort is not reflected in the benefit this might have for the users.
- We request the IASB to revise the disclosure requirements. In our view, especially the reconciliation (Paragraph 117) should be waived, not just in interim financial statements but also in annual financial statements.

Below we address the issues which are of special relevance to us:

Q1 and Q3: Performance obligations over time
We appreciate the distinction between revenue recognition over time and at a point in time. In this manner, the approach of revenue recognition remains the same concerning the principles of IAS 11 for certain construction contracts and the principles of IAS 18 for certain services. Possibly, there should be more accurate criteria with regard to the distinction between “services” and “goods”. We believe that the principles of paragraph 35 and 36 should cover all cases in which revenue recognition over time occurs. However, it might be difficult to interpret the criterion “alternative use” according to paragraph 35 and paragraph 36. Furthermore, it has to be ensured with regard to paragraph 35 (b) (iii) that beside the contractually regulated “right to payment for perfor-
mance completed to date" also statutory payment claims will be considered. In total, it should be ensured that in case of specific long term projects (e.g. construction of large facilities, ships, airplanes, etc.) recognition of revenue over time is still possible. In addition, we see scopes of discretion and questions concerning the interpretation of certain issues, especially with respect to the collection of license fees and warranties. In particular, no significant changes regarding license agreements should occur compared to the current regulations.

In certain cases the choice of the right method to estimate the total amount of an agreement according to paragraph 55 can be difficult. We appreciate that in cases of difficult estimations a recognition in accordance with the ZPMM (zero profit margin method) as specified in paragraph 48 is still possible. In this respect, we also agree with the regulation of paragraph 81: The reporting entities should not be allowed to consider highly subjective amounts but only amounts which can be reasonably anticipated.

In addition, we assume that – because of materiality reasons – revenue recognition at a point in time is permitted even though the criteria to recognise revenue over time are fulfilled.

**Question 2: The impairment loss shown straight under the revenue line items**

We do not agree with the proposals contained in paragraph 68 and 69. The presentation of impairment losses straight under the revenues suggests a direct link between the impairment loss and the revenues. In the majority of cases, this may not be true because subsequent impairment losses related to revenues of previous financial years are also recognized in this item. The necessity of subsequent corrections of impairment losses results from incurred losses after the date of fulfillment of the contract. This also applies in light of the fact that the discussion concerning the valuation of trade receivables still continues (IFRS 9).

For this reason, we do not see any benefit in such a presentation. In fact, this kind of presentation can lead to a distorted view on the revenue of an entity.
Therefore (because of the concomitant disadvantages of impairment losses presented as proposed) we believe that the users of financial statements would only consider the gross revenue as a relevant amount. As a result, we recommend to present impairment loss as before.

**Q4: Onerous test**

Our fundamental view is that the onerous test is more appropriate on contract level than on performance obligation level. A review of performance obligations involves a high workload compared to the potential benefit for the users of financial statements, i.e. we cannot understand the use in recognising an expense for a single performance obligation when the contract is profitable in its entirety. In spite of that, we agree with the recognition of expenses in accordance with IAS 11.36. Accordingly, only contracts with revenue recognition over time should be taken into account.

**Question 5: Required disclosures**

Even though the board proposes the interim statement notes to be dependent on materiality, we think the scope of the required notes is too capacious and causes extensive administrative burden in relation to the benefit of the users. The general requirement to present important information is already included in IAS 34.15. From our point of view solely the requirement of presenting a disaggregation of revenues and information about onerous performance obligations in the annual financial statements are acceptable.

In total, it is questionable whether there is an adequate balance between benefits and costs for the preparation of the notes. We would appreciate a significant reduction of the required disclosures.

**Question 6: Application of the proposed concept to account the transfer of non-financial items**

We understand the board’s approach to implement a standardised revenue recognition concept which is also applicable to other parts of the IFRS. However, we believe that the current regulation is a generally accepted and func-
tioning system. In particular, possible negative effects caused by a potential amendment of these regulations are currently not foreseeable, i.e. under which circumstances the “transfer of control” concept leads to different results than the current regulation in particular cases.

Additional 1: Allocating the transaction price to separate performance obligations

The solution of allocating the transaction price to separate performance obligations contem- plated by the board is quite understandable from our point of view. In our opinion it leads to sensible outcomes. Nevertheless, we consider the allocation of the transaction price to separate performance obligations to be only necessary for a few industrial sectors. Therefore we would appreciate a preceding materiality check which might render the allocation of the transaction price to separate performance obligations unnecessary. In this context the benefit of the users of the financial statement should serve as a criterion.

Additional 2: Retrospective application

We disagree with a retrospective application. A retrospective application would lead to a reassessment of all current contracts which would cause an enormous administrative effort. In our opinion there is no appropriate balance between the user’s benefits and the reporting entity’s incurring costs. In some cases, the required ascertainment for previous periods might not be feasible. Furthermore, a retrospective application results in an unnecessary burden since for example it might lead to a recurrence of revenue recognition in completed contracts (from which revenues have already been completely recognized). So, in our view, it is sufficient to apply the regulation to all prospectively closed contracts.

Best Regards,

Dr. Ingrun-Ulla Bartölke