

DP Revenue Recognition Comment Letters International Accounting Standards Board 30 Cannon Street London EC4M 6XH United Kingdom

23 June 2009

Dear Sir/Madam,

DP Preliminary views on revenue recognition in contracts with customers

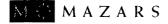
Mazars welcomes the opportunity to comment on the Discussion Paper (DP) Preliminary views on revenue recognition in contracts with customers. Our general comments are given below. Answers to the specific questions included in the DP are given in the Appendix.

We appreciate the work made by the IASB and believe it is a useful contribution.

However, we have serious concerns about the following points:

- 1. We believe that the current revenue recognition models proposed in IAS 11 and IAS 18 are relevant, because they provide useful information on an entity's performance to users of financial statements. We are not aware of users' needs that would require developing a new recognition model. However, we acknowledge that there is a need for guidance, especially in multiple element arrangement contracts.
- 2. Although we support the IASB's objective to develop a revised standard based on a unique revenue recognition model, we are not sure that this objective is achievable. In particular, we note that the scope of the DP would exclude financial instruments, insurance contracts and lessor accounting. Therefore, it appears there would not be a unique model. While we agree on these scope exclusions, we would encourage the IASB to clarify the potential impacts of the DP on the accounting for financial instruments, insurance contracts and lessor accounting.
- 3. Above all, the DP does not demonstrate that the revenue recognition model as drafted provides more useful information to users. In our view, and in accordance with the framework, the IASB should first determine what the revenue recognition concept should capture in order to reflect the entity's performance. We believe that, for long term contracts especially, "revenue" should reflect the progress of an entity in fulfilling its obligations in contracts with customers. Therefore, we do not think revenue should be recognised only when there is a transfer of the control of the assets.

Plaxity:



- 4. We note that for many construction contracts and other long term contracts, the principles proposed in the DP could lead to deferring revenue recognition until the contract is completed. We do not support the proposals as currently drafted in the DP because we believe revenue would not reflect the entity's performance and thus would not be decision-useful to users. We believe that in such contracts with customers, revenue should be recognised by reference to the stage of completion, because this method provides better and more useful information to users.
- 5. Lastly, we think that the "transfer of control" notion as described in the DP is complex and subjective to use, especially for rendering of services. We are not convinced that this notion is an improvement compared to the current "transfer of risks and rewards" notion.

We would be pleased to discuss our comments with you and remain at your disposal should you require further clarification or additional information.

Yours sincerely

Michel Barbet-Massin

Head of Financial Reporting Technical support



Appendix to our letter on IASB DP "Revenue Recognition". Answers to the specific questions raised in the invitation for comments

Chapter 2: A contract-based revenue recognition principle

Question 1: Do you agree with the boards' proposal to base a single revenue recognition principle on changes in an entity's contract asset or contract liability? Why or why not? If not, how would you address the inconsistency in existing standards that arises from having different revenue recognition principles?

Question 2: Are there any types of contracts for which the boards' proposed principle would not provide decision-useful information? Please provide examples and explain why. What alternative principle do you think is more useful in those examples?

Although we support the IASB's objective to develop a revised standard based on a unique revenue recognition model, we do not agree with the board's proposal to base a single revenue recognition principle on changes in an entity's contract asset or liability.

Currently, under IAS 11, an entity recognises revenue under a long term construction contract using the percentage of completion method, based on work completed to date. We believe this method provides useful information on the extent of contract activity and performance during a period.

We note that for many construction contracts and other long term contracts, the principles proposed in the DP could lead to deferring revenue recognition until the contract is completed. We do not support the proposals as currently drafted in the DP because we believe revenue so recognised would not reflect the entity's performance and thus would not be decision-useful to users.

According to the framework, the objective of financial statements is to provide information about the financial position, performance and changes in financial position of an entity that is useful to a wide range of users in making economic decisions.

We think the IASB should first determine what the revenue recognition concept should capture in order to reflect the entity's performance. In our view, revenue recognised under a contract with a customer should reflect the progress of an entity in fulfilling its obligations, and not merely the transfer of control on the assets.

We do not believe revenue recognition models in IAS 11 and IAS 18 are contradictory. In our view, the revenue recognition model in IAS 18 for sale of goods is a practical way to recognise revenue because for many sales of goods, there is no need to reflect the progress of an entity in fulfilling its obligations when the good is manufactured on a short period and in large quantities on a repetitive basis.



We think that, in developing the new model, the IASB has failed to identify the appropriate assets and liabilities whose changes would reflect the entity's performance. We propose a revenue recognition model based on the increase in assets that the entity manufactures (similar to a stage of completion method based on costs). As a practical simplification, we believe that for products that are manufactured on a short period and in large quantities on a repetitive basis, the revenue recognition model could be based on the increase in the entity's net contract asset.

We also believe the stage of completion method has two additional advantages:

- It will avoid debates on whether the contract is a sale of good or a rendering of service and whether the control on the asset/service is transferred to the customer on a continuous basis. Guidance given in the DP proves that this matter is complex and subjective (see question 8).
- It is already known and applied.

Question 3: Do you agree with the board's definition of a contract? Why or why not? Please provide examples of jurisdictions or circumstances in which it would be difficult to apply that definition.

We agree with the Board's definition of a contract. We note that IAS 32 incorporates already a definition. We believe both definitions should be identical.

We encourage the IASB to specify the notion of "enforceable". We believe a contract exists only when the entity and the customer are irrevocably committed. We do not believe a contract exists if the customer can breach the contract without paying compensation for the work performed by the entity.

Chapter 3: Performance obligations

Question 4: Do you think the boards' definition of a performance obligation would help entities to identify consistently the deliverables in (or components of) a contract? Why or why not? If not, please provide examples of circumstances in which applying the proposed definition would inappropriately identify or omit deliverables in (or components of) the contract.



Question 5: Do you agree that an entity should separate the performance obligations in a contract on the basis of when the entity transfers the promised assets to the customer? Why or why not? If not, what principle would you specify for separating performance obligations?

Question 6: Do you think that an entity's obligation to accept a returned good and refund the customer's consideration is a performance obligation? Why or why not?

Question 7: Do you think that sales incentives (e.g. discounts on future sales, customer loyalty points and "free" goods and services) give rise to performance obligations if they are provided in a contract with a customer? Why or why not?

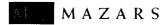
We think the Board's definition of a performance obligation would help entities identify the different components of a contract in most cases. We agree with the Board that an entity should identify the different performance obligations in a contract, especially in multiple delivery arrangements.

However, the definition of a performance obligation as drafted in the DP is not always easy to apply. We believe that in a sale of good with a legal warranty or a return right, the legal warrantee and the return right are clearly different deliverables from the sale of good. But we do not believe that these deliverables should automatically be identified as separate performance obligations. Indeed, in our view, a performance obligation should be separately identified when a separate sale of the deliverable underlying the performance obligation is feasible. Thus, deliverables that are incidental to a main deliverable should be combined in a single performance obligation.

This would provide more useful information to users, as performance obligations would be identified taking into account the substance of the transaction. We do not believe that identifying systematically all the deliverables would give useful information to users of financial statements.

Under this view, legal warranty would clearly relate to the initial sale and would be considered incidental to that sale. Thus, revenue would be recognised in full when the good is delivered, and the warranty costs would be recognised as a liability (within the scope of IAS 37). The same rationale would apply to return rights, as they clearly relate to the initial sale. However, in this last case, revenue would be recognised only if the initial sale meets all the criteria for revenue recognition. Therefore, a sale in which probability of return is significant would not meet the criteria for revenue recognition.

On the contrary, an extended warranty does not relate to the initial sale but to a future service that is specifically negotiated between the buyer and the seller. Likewise, sales incentives (e.g. discounts on future sales, customer loyalty points and free goods and service) clearly relate to a future sale or service. Thus, extended warranty and sales incentives would be identified as separate performance obligations.



We also think it should be pointed out that the identification of performance obligations should only be made if the effect is material to the financial statements.}

Question 8: Do you agree that an entity transfers an asset to a customer (and satisfies a performance obligation) when the customer controls the promised good or when the customer receives the promised service? Why or why not? If not, please suggest an alternative for determining when a promised good or service is transferred.

We note that under IAS 18, sale of goods depends largely on when the risks and rewards of ownership of the goods are transferred to the customer. We think this notion is applied consistently by entities and has proved to be a sound notion.

The DP proposes to recognise revenue for sale of goods when the customer controls the goods. We are not sure the notion of control is better than the notion of risks and rewards. In particular, for sale and repurchase agreements or consignment sales (as defined in the appendix of IAS 18), the DP would appear to concluding that control has been transferred and that a sale has taken place. But we believe that arrangements where risks and rewards have not been transferred are not sales in substance. Thus, we wonder whether both notions of risks and rewards and control should be retained in order to recognise revenue.

Furthermore, for a construction contract where the control of the asset is not transferred continuously, we do not believe that revenue should be recognised only when the customer controls the asset (see question 1).

Under current IAS 18, revenue relating to rendering of services is recognised by reference to the stage of completion of the transaction. The DP proposes to recognise revenue when the customer receives the promised service (or access to the promised service). We believe the notion of control as defined in the DP is complex and may be subject to different interpretations when applied to rendering of services. We foresee problems of consistency in implementation if no further guidance is given. In fact, we believe some service contracts do not necessary involve a continuous transfer. For instance, for consulting services, would the transfer of control occur at the delivery date of the final version of the report, or would it occur partly at intermediate stages?

Lastly, we think the DP does not provide clear principles to distinguish between sale of goods and rendering of services. We note that according to the DP, customisation of a good is an indicator that the contract may be for services, but other factors are to be considered (contract terms including payment terms, customer acceptance, operation of law...). We believe the principles given by the DP are not sufficient to be able to distinguish between a service and a good, particularly in agreements where a rendering of services comes with the physical delivery of a good.

We also note that construction contracts meet some of the indicators given by the DP to be analysed as contract for services. This is the reason why transfer of control of the asset/service in a construction contract is difficult to analyse (as for service contracts).



We think that the stage of completion method for construction contracts:

- avoids debates on whether the contract is a sale of good or a rendering of service and then whether transfer of control is continuous or not;
- gives better information to users of financial statements (see question 1).

Question 9: The boards proposed that an entity should recognise revenue only when a performance obligation is satisfied. Are there contracts for which that proposal would not provide decision-useful information? If so, please provide examples.

See question 1.

Chapter 5: Measurement of performance obligations

Question 10: In the boards' proposed model, performance obligations are measured initially at the original transaction price. Subsequently, the measurement of a performance obligation is updated only if it is deemed onerous.

Do you agree that performance obligations should be measured initially at the transaction price? Why or why not?

Yes, we do. We believe that measuring the performance obligations at the transaction price is objective and simple, and provides useful information to users.

Do you agree that a performance obligation should be deemed onerous and remeasured to the entity's expected cost of satisfying the performance obligation if that cost exceeds the carrying amount of the performance obligation? Why or why not?

Yes, we do. We believe that this is consistent with the definition of a liability (i.e. a present obligation, the settlement of which is expected to result in an outflow of resources embodying economic benefits). We note that this is also consistent with the existing IAS 37 and existing practice.

Do you think that there are some performance obligations for which the proposed measurement approach would not provide decision-useful information at each financial statement date? Why or why not. If so, what characteristic of the obligations makes that approach unsuitable? Please provide examples.

Do you think that some performance obligations in a revenue recognition standard should be subject to another measurement approach? Why or why not? If so, please provide examples and describe the measurement approach you would use.



No, we do not. In particular, for contracts in the scope of the DP (including construction contracts), we believe that performance obligations should not be remeasured, unless they are onerous. Indeed, we believe remeasurement is complex and brings volatility in the revenue line. We are not convinced a remeasurement approach would be decision useful to users. We think that the Board could rather require disclosures about the main changes in circumstances affecting the performance obligations.

However, we acknowledge that the allocated transaction price approach as drafted in the DP may not be appropriate for financial instruments and insurance contracts. Thus, we believe those contracts should be excluded from the scope of a revenue recognition standard.

Question 11: The boards proposed that an entity should allocate the transaction price at contract inception to the performance obligations. Therefore, any amounts that an entity charges customers to recover any costs of obtaining the contract (e.g. selling costs) are included in the initial measurement of the performance obligations. The boards proposed than an entity should recognise those costs as expenses, unless they qualify for recognition as an asset in accordance with other standards.

Do you agree that any amounts an entity charges a customer to recover the costs of obtaining the contract should be included in the initial measurement of an entity's performance obligations? Why or why not?

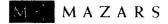
In what cases would recognising contract origination costs as expenses as they are incurred not provide decision-useful information about an entity's financial position and financial performance? Please provide examples and explain why.

We agree that any amounts an entity charges a customer to recover the costs of obtaining the contract should be included in the initial measurement of an entity's performance obligations.

We also agree that an entity should recognise contract origination costs as expenses as they are incurred unless they qualify for recognition as an asset in accordance with other standards.

In our view, expenses are recognised as an asset if:

- a contract specifically provides that the customer is paying for the entity's costs of obtaining a contract (cf. IAS 2);
- they are part of the cost of an internally generated intangible asset that meets the recognition criteria (cf. IAS 38 § 51 s.). Such expenses need to be directly attributable, i.e. they are not part of the general expenses of the entity.



We think success fees or commissions paid by the entity upon the customer's signature of the contract should always meet the recognition criteria in IAS 38. Thus, these costs should be capitalized and amortised over the contract's period in parallel with the revenue being recognised. Other pre-contract costs should be capitalized only from the date the entity meets the criteria under IAS 38, i.e. notably when the signature of the contract is highly probable and the entity can demonstrate the existence of future economic benefits.

Question 12: Do you agree that the transaction price should be allocated to the performance obligations on the basis of the entity's stand-alone selling prices of the goods or services underlying those performance obligations? Why or why not? If not, on what basis would you allocate the transaction price?

Question 13: Do you agree that if an entity does not sell a good or service separately, it should estimate the stand-alone selling price of that good or service for purposes of allocating the transaction price? Why or why not? When, if ever, should the use of estimates be constrained?

We agree that the transaction price should be allocated to the performance obligations on the basis of the entity's stand-alone selling prices. We believe this method could be easier to apply, if the performance obligations are determined as proposed in our answer to question 7. In fact, in that case, most of the stand-alone selling prices of the goods or services underlying the performance obligations should be observable or measurable.

Concerning construction contracts, we believe the same principles should apply. Let's take the example of a non-cancellable contract in which a supplier has to construct 20 missiles for the State. Missiles are to be delivered over a period of 3 years. Fixed payments are due on the delivery of each missile. But costs related to the construction of each missile decrease over the 3 year period because of economies of scale and suppliers' growing experience. The contract also contains a maintenance period of 5 years following the missiles' delivery. We believe each missile is a performance obligation (as they are delivered at different times). Maintenance is also a separate performance obligation. In our view, revenue relating to each missile should be recognised under the stage of completion method as the contract progresses (see question 1). We believe that, under the Board's proposed model, the transaction price should be allocated to each missile and to the maintenance deliverable on the basis of the stand-alone selling prices of the missile and the maintenance deliverable.

In that case, if the Board was to maintain its revenue recognition model, we encourage the IASB to deal with the issue of the margin recognition on such contracts. We do not believe the margin rate attached to each performance obligation should be different when the deliverables underlying those performance obligations are identical, unless inefficiency costs are incurred. Thus, in a non-cancellable contract negotiated globally, the margin rate attached to each missile delivered should be the same, although costs incurred for the construction of each missile may be decreasing because of economies of scale.