

#### **PREMABLE**

The Keppel Group is in the Offshore & Marine, Infrastructure and Property businesses.

Keppel is the leader in offshore rig design, construction and repair, ship repair and conversion and specialised shipbuilding. It is supported by a global network of 20 yards and offices in the Asia Pacific, Gulf of Mexico, Brazil, the Caspian Sea, Middle East and the North Sea regions.

As a leading global provider of environmental solutions and engineering services, Keppel offers a complete range of water and thermal technologies for municipal and industrial clients. In our energy business, we have a track record of developing, owning and operating power plants in Singapore, Asia and Latin America. We are also a leading service provider in logistics and data centres businesses within Southeast Asia and Europe.

Our property division contributes to changing cityscapes across Asia as a choice developer with a portfolio of residential developments, integrated townships and investment-grade commercial properties.

Majority of our businesses currently uses the Percentage of Completion (POC) method for revenue recognition, which in our view, faithfully represents the economic substance of the underlying business activities.



#### COMMENTS AND RESPONSES TO QUESTIONS RAISED IN PARAGRAPH IN38 of ED

### **Question 1:**

Paragraphs 35 and 36 specify when an entity transfers control of a good or service over time and, hence, when an entity satisfies a performance obligation and recognises revenue over time.

Do you agree with that proposal? If not, what alternative do you recommend for determining when a good or service is transferred over time and why?

#### **Comments**

There are 2 criteria for recognition of revenue over time i.e. Para 35(a) and Para 35(b).

Para 35 (a) is that the entity's performance creates or enhances an asset that the customer <u>controls</u> as the asset is created or enhanced. Control is defined in Para 32 with examples given in Para 32(a) to 32 (f).

- Does fulfilling any one of the criteria in 32(a) to 32(f) mean that we can recognise revenue over time? For instance, in the case of rig business, customer is able to pledge the work in progress and hence fulfil Para 32(e) but may not be able to meet the other criteria.
- With respect to the definition of control in Para 32 and BC85, more clarity should be given on the definition of 'the ability to direct the use of the asset'. For instance:
  - In the case of the real estate business, prior to completion of the construction, the buyer only has the Sale & Purchase agreement and not the property asset per se. However, he is able to either pledge the asset i.e. meet Para 32 (e) or to sub-sale i.e. meet Para 32 (d). Would the definition of 'ability to direct the use of the asset' be then considered as satisfied?
  - For rig business, if customer is able to take over WIP and pay for performance to date, would we satisfy Para 32 definition of customer having control?
- We would like to include <u>customer's acceptance of the work done to date</u> as one of the factors of control in Para 32. While Para 37(e) discusses about the customer's acceptance, it is not clear if this will be applicable in the case of rig building where customer will certify the work done and where required, request changes to the WIP.

Para 35 (b) requires that the entity's performance does not create an asset with an alternative use to the entity and at least one of the criteria in Para 35(b)(i) to (iii) is met.

• In the case of rig building, can the rig be considered as having no alternative use as long as there are contractual terms to prevent it from being transferred to another customer? However, when the customer defaults, the asset can be channelled to another customer. There could also be situations where the entity decides to complete the rig itself or make modifications to it such that they can sell the vessel



alternatively. We feel that the Board should include an example on rig or ship building to clarify on this.

- There should be more clarity on whether Para 35(b)(ii) applies to both tangible and intangible assets. Based on the existing draft of this Para, it appears that revenue would be recognised progressively on most contracts whereby the asset created has no alternative use as long as the entity continuously construct the asset. This is because another entity would not need to substantially re-perform on the work done by the entity to date.
- We would like to obtain clarification on Para 35(b)(iii), as interpretation of this criterion appears to be broad. It states that the entity has a right of payment for performance completed to date and in the event of contract termination, the seller is able to obtain compensation for recovery of its cost plus a reasonable profit margin. Typically, a profit margin would have been included in the total selling price and the contract would include protective clauses to recover the selling price based on the milestones should the contract be terminated, e.g. the right to sue the counterparty in pursuit of payment. Hence, it appears that the criteria in Para 35(b)(iii) can be loosely satisfied in most circumstances.



#### **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?

#### Comments

The current method of presenting doubtful debt provision as an operating expense is preferred for the following reasons:

- As impairment of receivables would typically be assessed in subsequent years (after revenue is recognised), there will be a mismatch between revenue and impairment expense for the period.
- According to the Board's basis of conclusion, the credit terms granted to customers and
  any impairment of the receivable is deemed similar to a change in transaction price and
  hence should be reflected as part of gross margin. This rationale seems to be more
  applicable to instances whereby cash rebates are given to customers.
- The proposed treatment of the ED may result in anomalous presentation, whereby there
  is no revenue in a given period but a credit risk expense arising from revenue recognised
  in previous periods.



#### **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?

### **Comments**

Broadly agree with the proposed constraint on revenue.



#### **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?

#### Comments

Do not agree that the scope of onerous test be restricted to only performance obligations that are satisfied over time and more than a period of one year.

What happens if entity has a contract that comprises solely of performance obligations that are satisfied at a point in time which is considered onerous? Will they have to defer recognition of the contract loss until contract completion? This will have an impact on the faithful representation of the financial statements if the effects of such onerous performance obligations are significant.



### **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.

#### **Comments**

Providing information on onerous contracts could pose an issue with confidentiality, especially if explanations are included to explain the rationale of entering into such contracts.

The disclosures are also too extensive, especially if it is to be prepared during interim periods. It may not be useful to the readers and the board should consider the cost and benefit of such disclosures.

In the case of the disaggregation of revenue, it is also not clear on whether the current segment reporting requirements for listed companies under FRS 108 is sufficient to meet the disclosure requirements in the ED.



#### **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?

#### **Comments**

Generally agree.

Same control and measurement principles to be applied to such transactions so that there is greater consistency, and fewer standards to refer to means reduced potential for accounting diversity.

However, the accounting for such a transfer will differ from that which is part of the ordinary activities i.e. record gain/loss instead of revenue and expense.



#### **ADDITIONAL QUERIES**

### **Question 7: Identification of separate performance obligations**

Identification of separate performance obligations - Para 28 states that a good or service is distinct if either (a) the entity regularly sells the good or service separately; or (b) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer. Para 29 also defines the criteria whereby an entity may account for a bundle as a single performance obligation.

In the case of the property business,

- Furnishing vouchers or subsidies may be given together with a sale of a unit.
- Golf memberships are sometimes included in the sale of property and buyers have an option to either take the membership ahead of time or upon completion.

More clarity should be given on whether such furnishing subsidy and free golf membership should be considered separate performance obligations. We feel that the Board should make it clear that Para 28 should be seen in connection with Para 10 and Para 1 which makes reference to an entity's ordinary activities. If the sale of the good or service is not part of an entity's ordinary activities, then it should not be considered as a distinct performance obligation.



### **Question 8: Time Value of Money**

The ED requires an entity to adjust for the time value of money in contract where the financing component is significant.

- There are contracts with various types of payment terms (upfront payment, deferred payment and progressive payment). For instance, in the case of upfront payment by the customer (i.e. entity is receiving financing from customer), do we need to also adjust for the time value of money?
- If upfront payment or deferred payment arrangements are the general practices of the industry or of the entity at the point of contracting, we are of the opinion that they are not financing arrangements and should not require adjustment for time value of money. We would like the Board to clarify on this.
- We would also like to clarify with the Board on whether interest cost is to be accounted for as a period cost or as part of the development/construction cost given that such arrangements are typically industry practices which may change from time-to-time.



### **Question 9: Guarantees by the seller**

Some contracts for the Offshore and Marine business include <u>refund guarantees</u> whereby in the case of default by the entity, an amount will be payable to the customers (this would be imposed only after serving a grace period subsequent to default on the agreed delivery date).

• There is no specific mention in the ED on refund guarantees. Is Para 57 which provides guidance on refund liability applicable to such refund guarantees?

In the case of the property business, there could be cases (for e.g. in Indonesia) where the bank gives loan to the buyer and the developer is then required to give a <u>guarantee</u> to the bank.

• In such cases, will Illustrative Example 7 be applicable?

The Board should give more clarification on the accounting for such guarantees.



#### **Question 10: Marketing expenses**

Can marketing costs be capitalised as part of WIP/project cost? Para 91 states that an entity shall recognise an asset only if those costs relate directly to a contract. Para 94 also states that an entity shall recognise as an asset the incremental costs of obtaining a contract with a customer if the entity expects to recover those costs".

However, in the case of the real estate business, marketing expenses (such as advertisement costs) are often incurred as publicity for the new property launches. These marketing efforts are considered essential in creating market awareness for the property launches, which indirectly aids in securing individual sales contracts with customers. While it cannot be directly attributable to each contract, it can be <u>directly attributable to specific property projects</u>. Hence we feel that such marketing expenses should be included as part of total contract costs.

Submitted by : Paul Tan

**Group Controller** 

**Keppel Corporation Limited** 

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