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Sent electronically through the IFRS Foundation website (www.ifrs.org)

30 March 2012

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sirs,

IASB Exposure Draft "Revenue from Contracts with Customers" as issued in November 2011 (A revision of ED/2010/6)

We continue to support the Boards' proposal to develop a single principle-based revenue recognition model on contracts with customers. We welcome the Boards' effort to clarify and simplify the proposals based on the feedback received. We also recognise that some of the concerns and proposed changes stated in our previous submission have been addressed. However, we strongly believe that some of the principles require further clarification and amendment before they can be adopted effectively.

Our detailed responses to the specific questions set out in the revised Exposure Draft are appended to this letter. The key areas which we urge the Boards to consider making changes to are as follows:

<u>Criteria for performance obligation satisfied over time</u>

We consider the newly specified criteria in the revised ED more easily applicable to certain industries such as the construction business but less clear in the assessment of the sale of property by real estate developers in particular where units are pre-sold.

As proposed in the revised ED, an entity shall firstly test whether a performance obligation is satisfied over time based on certain criteria. If an entity does not satisfy a performance obligation over time, then the performance obligation is satisfied at a point in time. Under the first test, one of the criteria for determining if the transfer of control of a good or service occurs over time is that "the entity's performance does not create an asset with an alternative use" and "has a right to payment for performance completed to date". We consider these criteria unclear. To avoid unnecessary ambiguity, the Boards must provide further clarification on the alternative use assessment and the concept of right to payment for performance completed to date. In particular, the change in the concept of "transfer of control" may result in unintended early revenue recognition on pre-sold properties in mainland China and Hong Kong.

Currently, it is our Group's policy to recognise revenue from a sale on the transfer of the significant risks and rewards of ownership in accordance with IFRIC 15. This usually occurs when a property is delivered to a customer. When development units are pre-sold, revenue

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is also recognised upon the handover of the units to the customers regardless of the different payment options selected by the customers. This is similar to satisfying a performance obligation at a point in time. We consider that this accounting treatment best reflects the economic substance of the transactions based on the facts and circumstances surrounding the contracts with customers in mainland China and Hong Kong.

Presentation of impairment loss related to contracts with customers

We do not support the proposed presentation of impairment losses related to contracts with customers as a separate line adjacent to the revenue line in the profit or loss account. Such impairment losses should be presented as an expense and not a "deduction" from revenue. We believe the current presentation of impairment losses as an operating expense fairly reflects the substance of how entities manage and monitor customer default risk.

Disclosure requirements for Interim Reporting

We disagree with the proposed additional disclosure requirements for interim reporting which appear to be rule-based. We consider that the current disclosure requirements under the principled-based IAS 34 "Interim Financial Reporting" adequately provide useful and relevant information to users. If this is an area of concern, the Boards should conduct a comprehensive review of IAS34 instead of introducing piecemeal disclosure requirements for interim reporting at an individual standard level.

If you have any questions on the content of this letter, please do not hesitate to contact me.

Yours faithfully,

James Riley
Group Finance Director

c.c. Hong Kong Institute of Certified Public Accountants

About the Jardine Matheson Group

Founded as a trading company in China in 1832, Jardine Matheson is today a diversified business group focused principally on Asia. Its interests include Jardine Pacific, Jardine Motors, Jardine Lloyd Thompson, Hongkong Land, Dairy Farm, Mandarin Oriental, Jardine Cycle & Carriage and Astra. These companies are leaders in the fields of engineering and construction, transport services, insurance broking, property investment and development, retailing, restaurants, luxury hotels, motor vehicles and related activities, financial services, heavy equipment, mining and agribusiness. The Group had revenues (including the revenues of associates and joint ventures) of US$57 billion in 2011 and total assets of US$58 billion at the end of 2011. It employs some 330,000 people.

Jardine Matheson Holdings Limited is incorporated in Bermuda and has a premium listing on the London Stock Exchange, with secondary listings in Bermuda and Singapore.

Jardine Matheson is one of the pioneers in adopting International Financial Reporting Standards, having first prepared its financial statements in accordance with IFRS in 1990.

APPENDIX

Comments on questions set out in the revised ED "Revenue from Contracts with Customers"

> Question 1
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> *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?*

We generally support the Boards' revised proposal which specifies criteria to determine whether the transfer of a good or service occurs over time or at a point in time. However, we urge the Boards to clarify and reconsider the criteria under paragraphs 35 and 36 in respect of the transfer of control of a good or service over time. While these criteria appear to be more easily applicable to certain industries such as the construction industry, it is less clear when evaluating others, in particular real estate development where units can be pre-sold.

As proposed in the revised ED (para 34), an entity shall firstly apply paragraphs 35 and 36 to determine at contract inception whether a performance obligation is satisfied over time by transferring control of a promised good or service over time. If not, then the entity satisfies the performance obligation at a point in time in accordance with paragraph 37.

In accordance with the current requirements under IAS 18 "Revenue" and IFRIC 15 "Agreements for the Construction of Real Estate", it is our Group's accounting policy to recognise revenue from the sale of properties on the transfer of the significant risks and rewards of ownership, which generally coincides with the time when properties are delivered to customers. When there are pre-sales of development units, revenue is still recognised at this single point in time, i.e. upon the handover of the units to the customers, instead of recognised over time even though customers may have selected different payment schedules. We consider that this accounting treatment best reflects the economic substance of the transactions based on the facts and circumstances surrounding the contracts with the customers.

However, with the new proposals in the ED, by going through the test under paragraphs 35 and 36 first, it is unclear if the existing accounting policy can still be applied. This change in the concept of "transfer of control" may result in unintended early revenue recognition on pre-sales of properties in mainland China and Hong Kong. In particular, we are concerned by the criteria to qualify a performance obligation as being satisfied over time:

"The entity's performance does not create an asset with an alternative use to the entity (para 35(b), 36)"; and "the entity has a right to payment for performance completed to date and it expects to fulfill the contract as promised (para 35 (b) (iii))". We believe the above criteria must be reconsidered to take into account our questions below.

- In the case of real estate development, it is important to consider if the buyer is able to specify the major structural elements of the design of the real estate at contract inception or during the construction when evaluating whether an asset has an alternative use. If the structural elements of the building design are specified by the buyer, it is less likely for the developer to "readily direct" the building to another customer. This consideration is currently stated in IFRIC 15. In Hong Kong, the buyers in most cases cannot specify the major structural elements of the unit's design.

- It is common for property developers in Hong Kong to offer buyers of units in the same building different choices of payment terms for marketing and funding purposes. In some

cases, a 10% deposit is paid upon signing of the contract and the balance is paid on handover of the unit. There are also cases when the buyers pay 100% of the purchase price on signing of the pre-sale contracts to benefit from an early bird discount being offered by the developer. It is unclear under the proposal how to apply the "right to payment for performance completed to date" concept with reference to the different payment methods.

- It is unclear how to assess the performances separately in respect of the land and building component of the property.

- It is common in Hong Kong that the buyer cannot cancel the transaction except in the case of default by the developer. If the buyer defaults, the developer has the right to sell the property (as the developer still owns the legal title of the property) in the market and pursue the buyer for the compensation of any loss of profits arising from such sale. The developer also has the right to sue the buyer for specific performance of the contract through legal action. It is unclear if the developer's right upon default by customer to redirect the use of the property should be considered as part of the substantive terms in the contract when assessing if there is alternative use for the asset. It is also unclear in the revised proposal whether the right to payment should take into consideration the legal right on default.

Our view is that the sale of property is no different from the sale of manufactured goods. The risk and rewards of the ownership of the property still remain with the developer until the delivery of the property to the buyer and hence, revenue can only be recognised at this point in time.

Question 2

Paragraphs 68 and 69 state that an entity would apply IFRS 9 (or IAS 39, if the entity has not yet adopted IFRS 9) or ASC Topic 310 to account for amounts of promised consideration that the entity assesses to be uncollectible because of a customer's credit risk. The corresponding amounts in profit or loss would be presented as a separate line item adjacent to the revenue line item. Do you agree with those proposals? If not, what alternative do you recommend to account for the effects of a customer's credit risk and why?

We do not agree with the proposed presentation of impairment losses related to contracts with customers as a separate line item adjacent to the revenue line item in the profit or loss account which implies a reduction in revenue. Such impairment losses should be treated as an expense and not a "deduction" from revenue.

Before entering into a sales contract with a customer, an entity will normally have evaluated the credit risk of the customer and taken this into account when pricing the contract and agreeing on a payment schedule. If there is a specific potential default case identified at the time when an entity obtains an unconditional right to receive consideration, we consider that the corresponding revenue amount should not be recognised. On the other hand, revenue should be recognised when the recognition and measurement criteria have been satisfied. The impairment losses incurred based on subsequent credit risk review of receivables from customers should be treated as an operating expense. Separate disclosure of the impairment of debtors is already required in accordance with IFRS 7 to provide relevant information to users in respect of the collectability of receivables from customers. In addition, if the impairment loss is related to previous financial year's sales, it would be misleading to present it adjacent to the current year's revenue.

<u>Question 3</u>

Paragraph 81 states that if the amount of consideration to which an entity will be entitled is variable, the cumulative amount of revenue the entity recognises to date should not exceed the amount to which the entity is reasonably assured to be entitled. An entity is reasonably assured to be entitled to the amount allocated to satisfied performance obligations only if the entity has experience with similar performance obligations and that experience is predictive of the amount of consideration to which the entity will be entitled. Paragraph 82 lists indicators of when an entity's experience may not be predictive of the amount of consideration to which the entity will be entitled in exchange for satisfying those performance obligations. Do you agree with the proposed constraint on the amount of revenue that an entity would recognise for satisfied performance obligations? If not, what alternative constraint do you recommend and why?

We agree with the proposed constraint on the amount of revenue that an entity would recognise for satisfied performance obligations.

<u>Question 4</u>

For a performance obligation that an entity satisfies over time and expects at contract inception to satisfy over a period of time greater than one year, paragraph 86 states that the entity should recognise a liability and a corresponding expense if the performance obligation is onerous. Do you agree with the proposed scope of the onerous test? If not, what alternative scope do you recommend and why?

We do not support the proposed scope of the onerous test on a performance obligation that is satisfied over a period greater than one year. The time span to satisfy a performance obligation should not be a criterion for onerous assessment. The proposed scope will lead to the omission of onerousness assessment on performance obligations to be satisfied in less than one year or performance obligation satisfied at a point in time. Accordingly, we also do not agree with the proposed scope out from IAS 37 "Provisions, Contingent Liabilities and Contingent Assets" the "right and obligations arising from contracts with customers" (as proposed in para D21). This will result in the non-recognition of material liabilities arising from contracts at the end of the reporting period.

In addition, we are not sure if it is practicable to apply the onerous test at performance obligation level in certain cases even though it is principally consistent with the revenue recognition model. An entity may enter into a contract which is profitable at a contract level but contains components at an individual performance obligation level that are intended to be loss making. In this case, the recognition of losses at individual performance obligation level does not reflect the economic reality of the contract with a customer and it may not provide meaningful information to users of the financial statements.

Accordingly, we consider that the recognition principle based on obligations under a contract in accordance with IAS 37 should be more appropriate and easier to operate in order to ensure the proper recognition of liabilities arising from contracts with customers.

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 (para D19 in Appendix D). 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 correspondence 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 fulfill 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.

We do not agree with the above proposed additional disclosure requirements in the interim financial reports. We consider that the current disclosure requirements under the principled-based IAS 34 "Interim Financial Reporting" adequately provide useful and relevant information to the users. In particular, IAS 34 (para 15) requires an entity to provide explanation and relevant disclosure of events and transactions that are significant to the understanding of the changes in its financial position and performance since the end of the last annual financial report. The proposed additional disclosure requirements appear to be prescriptive and not principled-based.

We suggest the Boards conduct a comprehensive review on IAS34, if needed, instead of introducing piecemeal disclosure requirements for interim reporting at individual standard level.

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 assets (paragraphs D17, D22 and D26 in Appendix D). Do you agree that an entity should apply the proposed control and measurement requirements to account for the transfer of non-financial assets that are not an output of an entity's ordinary activities? If not, what alternative do you recommend and why?

We agree with the proposal to apply a consistent control and measurement requirements to account for the transfer of non-financial assets that are not an output of an entity's ordinary activities.