12 June 2009

Sir David Tweedie Chairman International Accounting Standards Board 30 Cannon Street London EC 4M 6XH UNITED KINGDOM

commentletters@iasb.org.uk

Dear Sir David

"Revenue Recognition

The Group of 100 (G100) is an organization of chief financial officers from Australia's largest business enterprises with a purpose of advancing Australia's financial competitiveness. The G100 is pleased to provide comments on the Discussion Paper.

The G100 supports the development of principles-based Standards for recognition and measurement and believes that disclosure requirements of Standards should also be assessed against a set of disclosure principles.

As an overall view the G100, while agreeing with the objective of developing a single model for revenue recognition, does not believe that the proposals achieve the objective. The reliance on completion and delivery upon performance appears to be more based on the form of a transaction rather than its economic substance. The G100 believes that the recognition of revenue should reflect the performance of economic activities occurring under the contract as that activity occurs and the entity has claims against the customer. Decision-useful information for both users of financial statements and for management decision-making should reflect underlying economic activity.

Q1. 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? The G100 agrees with the proposal that there should be a single revenue recognition principle. However, the approach in the ED based on changes in an entity's contract asset or contract liability in respect of contracts within the scope of the ED is not comprehensive. The G100 considers that the principle should be expressed in terms of recognizing the changes in value arising from performing obligations under the contract which give rise to claims on the other party. A principle based on such an approach can be applied more generally than to contracts.

Q2. 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?

Yes. The application of the proposals on long-term and construction type contracts does not enable the economic substance of performance and the changes in value arising from that performance to be shown. The principle should reflect the pattern of economic activity under the contract which would be decision-useful information for users.

Q3. Do you agree with the Boards' 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.

Yes. The G100 considers that if this definition is adopted it should be applied across all Standards so there is no ambiguity arising from the use of different wording.

Q4. Do you think the Boards' proposed 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.

The definition of a performance obligation is supported in concept. However, further guidance will be needed if it is to be applied in practice. For example, in a construction contract the performance obligation may be interpreted as occurring at different stages of the contract. Performance may be determined on the basis of the whole contract or as parts of a contract. In these circumstances the allocation of the contract price to the respective performance obligations would present difficulties in interpretation and potentially impair comparability.

Q5. 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?

Yes. The G100 considers that a performance obligation can be performed/completed without the passing of legal title to the other party. For example, this would most frequently occur in long-term construction contracts where stages of completion are specified and when satisfied value transfers occur, even though legal title has not changed.

- Q6. 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? The G100 considers that the return by a customer evidences a failed sale. The return of goods is not expected in the normal course of events. Except in rare cases (product recalls etc) returns are not a significant item for companies and should be accounted for if and when they occur.
- **Q7.** Do you think that sales incentives (for example, 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?

This issue is, in part, addressed in IFRIC 13 'Customer Loyalty Programmes'. However, we consider that discounts on a future sale do create a performance obligation which the entity must honour should the customer exercise the right. The concern here is the reliability of measurement of the obligation.

Q8. 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.

The G100 generally agrees with this approach as consistent with the Framework definition of an asset. The transfer of resources to another entity evidences the completion of the performance obligation and signals the recognition of revenue. However, the reliance on the control concept is likely to present difficulties in interpretation and application because the notion of control is used in different contexts in Accounting Standards and depends on the facts and circumstances in each case. For example, it is not clear from the Discussion Paper how the notion of control would be applied in respect of long-term construction contracts.

Q9. The Boards propose that an entity should recognize 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.

This will depend on how the performance obligations under a contract are interpreted. If the performance obligation is interpreted as delivery of control of the asset to the purchaser upon completion the proposed approach would not provide decision-useful information in respect of long-term construction type contracts and service agreements. In these cases the economic substance is that value accrues as performance occurs during a contract.

- **Q10.** 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.
 - a. Do you agree that performance obligations should be measured initially at the transaction price? Why or why not?
 Yes. The entity earns revenue by undertaking activities in performance of its obligations under the contract.
 - b. 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. Remeasurement will be necessary in order to reflect the effect of impairment and/or the onerous nature of a contract on the margin on the contract.
 - c. Do you think that there are some performance obligations for which the proposed measuremens approach would not provide decisionuseful information at each financial statement date? Why or why not? If so, what characteristic of the obligations makes that approach unsuitable? Please provide examples. Yes. Contracts involving long-term construction type arrangements and some types of warranty obligations.
 - d. 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.

The G100 agrees with the proposals regarding initial measurement. However, our concerns relate to subsequent measurement particularly in respect of the satisfying performance obligations at various stages of long-term construction type contracts.

The G100 considers that a principle-based regime should be sufficiently robust to deal with a variety of contracts and circumstances. If exceptions are necessary this is indicative that the principle needs further consideration.

Q11. The Boards propose 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 (for example, selling costs) are included in the initial measurement of the performance obligations. The Boards propose that an entity should recognize those costs as expenses unless they qualify for recognition as an asset in accordance with other standards.

a. 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?

Yes. These costs form part of the total amount of the contract costs which the entity will seek to recover from the contract and should be recognized as an asset if they meet asset recognition criteria.

b. In what cases would recognizing 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.

These costs should be recognized as an expense where they do not meet asset recognition criteria.

The G100 believes that the treatment of these costs should be addressed in the context of a review of IAS 38 'Intangible Assets' because of difficulties arising in interpreting its requirements relating to contract origination or customer setup costs.

Q12. 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?

The G100 considers that the stand-alone price could be an appropriate basis of allocation where such prices are readily available for the separate performance obligations in a contract. We believe that this is likely to be the case in many circumstances and believe that the judgment whether to use a stand-alone price, management's estimate of such a price or a costs incurred basis is best left to management's assessment of the circumstances and the economic substance of the transaction.

However, there are significant practical issues associated with applying the proposed principles on the allocation of revenue to the various performance obligations that will make it difficult for companies to implement. This is particularly the case for high turnover items whose value or selling price changes regularly (eg mobile phones). Developing allocation models outside of the billing system to appropriately account for these items will be difficult and costly to implement because of the need to change those models due to constantly changing prices.

For example, Appendix A (examples 2 and 4) demonstrate that services revenue must be allocated to each period of service (generally each year) based on the costs to provide that service as estimated at the inception of the contract. This approach has the effect that the revenue is not recognized on a straight line basis, but rather is based on the expected cost profile. This may differ from actual experience. For example, in a contract to provide maintenance services for 3 years, revenue is allocated to each year based on expected costs, even though the customer is billed evenly over the 3 year period. This could result in revenue being deferred until year 3 if greater costs are expected in year 3. Disaggregating service contracts in this way would be extremely onerous for companies to implement, particular large scale outsourcing arrangements where equipment may also be provided.

Q13. Do you agree that if an entity does not sell a good or service separately, it should estimate the standalone 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?

This is particularly evident in respect of its effect on accounting for long-term construction type contracts where revenue and profit emerges as economic activity is undertaken and not as a single amount at the completion of a contract.

Yours sincerely

Tony ReevesNational President