

Summary of significant IASB tentative decisions made in relation to the IASB/FASB Revenue recognition project

1. The IASB and FASB (the Boards) are in the process of redeliberating their proposals in the light of feedback received on the Revenue ED. They have reached decisions on some significant aspects of the model and AASB staff have exercised judgement in identifying the issues that we thought should be brought to the attention of AASB members (as outlined in the table below). The table below incorporates the Boards' decisions up to 21-23 March 2011 meeting. AASB staff will provide a verbal report on any subsequent decisions. All decisions are tentative and subject to change.

AASB staff's comments and recommendation to AASB members on the tentative decisions made by the IASB and FASB are in paragraph 2 of this paper.

Significant issues	Snapshot of IASB/FASB tentative decisions	Broadly align with AASB views?
1) Combining contracts	The Boards have decided that contracts that are interrelated should be combined, if they are entered into at the same time and generally with the same party (or a related party) and other factors (such as commercial objective, consideration and goods and services) are interrelated.	Yes
2) Contract modification	If a contract modification results only in the addition of a distinct good or service at a price that is commensurate with that additional good or service, the entity should account for the contract modification as a separate contract.	Yes
3) Identifying separate performance obligations	An entity should account for a bundle of promised goods or services as one performance obligation if the entity provides a service of integrating those goods or services into a single item that the entity provides to the customer. If not, an entity should account for a promised good or service as a separate performance obligation if: a) the pattern of transfer of the good or service is different from the pattern of transfer of other promised goods or services in the contract; and b) the good or service has a distinct function. A good or service has a distinct function if either: i. the entity regularly sells the good or service separately; or ii. the customer can use the good or service either on its own or together with resources that are readily available to the customer.	Yes
4) Warranties	If a customer has the option to purchase a warranty separately from the entity, the entity should account for the warranty as a separate performance obligation. Otherwise, the entity should account for the warranty as a cost accrual (i.e. as per IAS 37) unless the warranty provides assurance to the customer other than the good or service was as specified in the contract.	Partly The AASB expressed concern about different measurement bases being adopted for similar items.
5) transaction price and credit risk	An entity should not reflect the effects of a customer's credit risk in the measurement of the transaction price and, hence, revenue. An entity would separately recognise any expected impairment loss on contracts with customers, with the loss presented as a separate line item adjacent to revenue, i.e. as contra revenue.	Partly Refer to paragraph 2(i) for details
6) Recognition of revenue from goods vs services	The Boards decided to have separate guidance for when transfers of goods and transfers of services occur.	No Refer to paragraph 2(ii) for details

Significant issues	Snapshot of IASB/FASB tentative decisions	Broadly align with AASB views?
7) Transfer of goods	<p>The Boards reaffirmed that a performance obligation to provide goods is satisfied when the customer obtains control of the goods.</p> <p>The Boards also decided to include ‘risk and rewards’ as an indicator of control on the basis that exposure to risks and rewards is a consequence of control. Thus there are now four indicators of transfer of control for goods:</p> <ul style="list-style-type: none"> a) The customer has an unconditional obligation to pay. b) The customer has legal title. c) The customer has physical possession. d) The customer has the risks and rewards of ownership. 	<p>Partly</p> <p>Refer to paragraph 2(iii) for details</p>
8) Transfer of services	<p>To recognise revenue for a service, an entity must determine that a performance obligation is satisfied continuously. An entity satisfies a performance obligation continuously if at least one of the following two criteria is met:</p> <ul style="list-style-type: none"> a) The entity’s performance creates or enhances an asset that the customer controls as the asset is created or enhanced; or b) The entity’s performance does not create an asset with alternative use to the entity¹ and at least one of the following is met: <ul style="list-style-type: none"> i) The customer receives a benefit as the entity performs each task. ii) Another entity would not need to reperform the task(s) performed to date if that other entity were to fulfil the remaining obligation to the customer iii) The entity has a right to payment for performance to date 	<p>Partly</p> <p>Refer to paragraph 2(iii) & iv) for details</p>

2. AASB staff’s comments and recommendation on some of the IASB’s tentative decisions:

- i. Transaction price and credit risk (item (5) in the table above) – the IASB has partly addressed the AASB’s concerns in its recent proposals by clarifying that entities should not reflect the effects of a customer’s credit risk in the measurement of revenue. However, the proposals also require entities to present any impairment loss on contracts with customers as a separate line item adjacent to revenue i.e. as contra revenue. We think that the IASB should reconsider this aspect of the proposal as the presentation requirement proposed will result in entities showing a net revenue amount as a subtotal on the statement of comprehensive income which is inconsistent with the AASB’s response to the ED and the IASB’s proposals on accounting for interest income and the impairment of loan contracts. The net revenue presentation may also impact many entities, for example in reviewing debt covenants and compensation metrics, recasting budgets and forecasts and changing systems and processes.
- ii. Recognition of revenue (item (6) in the table above) – having separate guidance for transfer of goods and services does not seem to be in line with the single revenue recognition principle objective of the project. We suggest that the IASB should keep to a single revenue recognition principle that is based on rights to consideration/payment as performance obligations are satisfied and provide indicators of when performance obligations may be satisfied for goods or services. This is consistent with the AASB’s response to the ED that ‘a customer’s unconditional obligation to pay an entity for work performed’ should be elevated to a higher status from being just an indicator for transfer of control.

1 “ An asset with alternative use to an entity is an asset that the entity could readily direct to another customer. In making that evaluation, an entity would consider the terms of the contract and also should consider the costs and consequences to the entity of directing the asset to another customer (e.g. whether the entity would incur significant costs to re-work the asset for the other customer or whether directing the asset to another customer would result in breach of a contract)”. – extracted from IASB meeting February 2011 staff paper (agenda item 4B).

- iii. Transfer of goods and services (item (7) and (8) in the table above) – the proposed guidance on when an entity satisfies a performance obligation continuously seems to address the AASB’s comment on the ED that the proposals need to focus more on the provision for services and provide more guidance on how the concept of control applies to services with or without a final deliverable. However, for both goods and services, we are concerned that the application of the proposals may result in revenue being recognised without the entity having a right to payment for the goods or performance to date. For example, a developer of off plan multi-unit properties may be able to recognise revenue as the units are being constructed even though the developer may not have a right to payment for performance to date. Consistent with our comments in (ii) above, we think that a right to payment for goods or performance to date should be a necessary condition to recognise revenue in all circumstances.
- iv. The term ‘alternative use to entity’ (item (8b) in the table above) should be clarified in the final standard to help prevent divergence in practice in interpreting the term. For example, some may consider that an entity has an alternative use for a standardised property that it constructs under contract with a customer as this property can be directed to another customer. Others may not agree as directing a property that is under contract with a customer to another (although the property is standardised) may result in a breach of contract.
- v. As a separate issue, we would like the IASB to be explicit about the IFRS that would apply to contract assets such as receivables. If the intention of the IASB is that such assets should be within the scope of the revenue standard and not the financial instruments standards, then the IASB should make this clear.

In the EFRAG IASB joint meeting on 18 March 2011, EFRAG provided similar comments to points ii – iv above on the Boards’ tentative decisions to date.

We recommend that the AASB write to the IASB on issues i – v above, which we consider to be significant and warrant a Board to Board communication.

Question to Board members:

- 1) Do you agree with staff’s comments in issues i – v in paragraph 2 above?
- 2) If yes, do you agree that a letter to the IASB should be prepared from the AASB and approved by the Chairman?