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22 June 2009

Dear Bruce

**Exposure Draft ITC 18 Request for Comment on IASB Discussion Paper *Preliminary Views on Revenue Recognition in Contracts with Customers***

I am enclosing a copy of the PricewaterhouseCoopers response to the International Accounting Standards Board's (IASB) Discussion Paper *Preliminary Views on Revenue Recognition in Contracts with Customers*. The letter reflects the views of the PricewaterhouseCoopers network of firms and as such includes our own comments on the matters raised in the Exposure Draft.

We support the introduction of a single, contract-based revenue recognition model, subject to our detailed comments in the enclosed letter. In our view, the proposals should result in financial statements that would be useful to users and would be in the best interest of the Australian economy.

We do not believe that there are any regulatory issues or other issues arising in the Australian environment that would affect the implementation of the proposals, particularly relating to not-for-profit entities and public sector entities.

We would welcome the opportunity to discuss our views at your convenience. Please contact me on (03) 8603 3868 if you would like to discuss this further.

Yours sincerely



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Financial Accounting Standards Board  
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**Re: File Reference No. 1660-100: Preliminary Views on Revenue Recognition in Contracts with Customers**

We are responding to the invitation of the IASB/FASB ("the boards") to comment on the above-mentioned discussion paper on behalf of PricewaterhouseCoopers. Following consultation with members of the PricewaterhouseCoopers network of firms, this response summarises the views of those member firms who commented on the discussion paper. "PricewaterhouseCoopers" refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

We welcome the opportunity to comment on the discussion paper. We agree with the boards' objective to clarify the principles for recognising revenue to provide clearer and more consistent guidance. We believe a single, contract-based revenue recognition model will help to achieve this goal. The proposed standard should increase revenue recognition consistency and better align revenue recognition principles with the conceptual frameworks. The boards have made good progress on the development of a single revenue recognition model, although we recognise there are significant issues yet to be addressed. Successful resolution of those issues is paramount to achieving the boards' objectives.

**Scope**

We believe that the proposed model should apply to most contracts with customers. However, we recognise that the boards are currently working on a number of projects (e.g., leases and insurance) that involve contracts and transactions that may be similar to those addressed by the revenue discussion paper. We believe that, for conceptual and practical reasons, such contracts should be addressed within those projects. We believe it is also important that the boards ensure consistency in the treatment of economically similar transactions regardless of the project in which they are addressed. The fundamental principles in this discussion paper, such as control, should be aligned to the extent possible with similar concepts in other projects.

**Definition of a contract**

We agree with the proposed definition of a contract but believe the boards could enhance the definition by better articulating a principle for determining what constitutes the contract (i.e., the unit of account to which the principles in this discussion paper should be applied). We believe this principle should be



designed to ensure the accounting reflects the economics of the arrangement between the parties. The principle should be sufficient to guide preparers on whether to combine contracts and how to treat contract options, modifications, renewals, and variations/change orders.

The boards' emphasis on the contract makes it important to differentiate between arrangements and contract terms that are substantive and those that lack commercial substance. We do not believe that a revenue standard should be applied to contracts and contract terms that lack commercial substance.

#### **Definition of performance obligations**

Performance obligations are the foundation for determining when revenue is recognised. Correctly defining performance obligations in a contract is therefore critical. We agree with the proposed definition of a performance obligation but believe it would be helpful for the boards to illustrate how the definition would be applied in the following key areas:

- implicit or constructive obligations established by past practice;
- statutory obligations;
- obligations that can be settled in cash or by delivering an asset; and
- obligations in service arrangements.

We acknowledge it would be challenging for the boards to consider every potential business arrangement. Application guidance, including examples that illustrate how the principle should be applied, would improve consistency in the identification of performance obligations.

#### **Satisfaction of performance obligations**

We agree with the concept that revenue results from the satisfaction of performance obligations. A single trigger will provide more consistency in revenue recognition, but only if it is supported by enhanced guidance on the identification of performance obligations and a clear principle for control transfer that ensures the economics of a transaction are reflected in the accounting. We are concerned that using a strict legal definition of control transfer, or one based only on physical control, could result in accounting that does not reflect the economic substance of transactions and provides less decision-useful information for users. The principle might state, for example, that control has transferred when the customer has the right to direct, use, or access at will the resource underlying the asset (whether a good or a service) so as to enjoy the economic benefits of that asset or preclude or limit its use by others. This principle should be accompanied by indicators of when control is transferred.

We envision that for many transactions, a 'control-trigger' model that reflects the underlying economics will result in revenue recognition in the same period as required under existing guidance. However, we recognise that in certain cases revenue recognition could occur at different times.

#### **Measurement of rights**

We agree with the boards' tentative conclusion that the measurement of the contract asset should be based on the transaction price as opposed to a current exit price. Although the boards did not address the measurement of contract rights in the discussion paper, this is a fundamental aspect of the proposed model that, depending on the outcome of the boards' deliberations, may impact other aspects of application of the proposed model.

#### **Remeasurement of performance obligations**

We do not believe performance obligations should be remeasured after initial allocation, except in situations where the transaction price has been adjusted. We do not agree with the boards' tentative conclusion to require remeasurement of a performance obligation when it becomes onerous. This is



because the proposed model uses the transaction price as the basis for measuring contract consideration and allocating consideration to performance obligations. We believe creating an onerous contract provision by remeasuring the performance obligation creates an exception to this model, as the performance obligation would be adjusted for an event other than a change in transaction price. The recognition and measurement of onerous contracts relate to the accounting for contract costs and the determination of whether a liability has been incurred. We therefore believe the existence, recognition and measurement of onerous contracts should be addressed in the liabilities standards.

### **Cost recognition**

We agree with the boards' tentative conclusion to exclude cost recognition guidance from the revenue standard. However, since the existing revenue literature in both frameworks includes cost recognition guidance in a number of instances, removal of this guidance may result in inconsistent treatment by preparers. We suggest that the boards evaluate the adequacy of the existing cost recognition standards to determine whether additional principles or guidance might be needed in those standards to address the recognition of customer contract related costs. For example, there is currently limited guidance on the accounting for amounts paid to third parties to obtain a contract with a customer or costs incurred in preparation for providing a service.

Our answers to the specific questions in the discussion paper provide more detail on the views expressed above and are attached in the Appendix to this letter.

If you have any questions in relation to this letter please do not hesitate to contact Richard Keys (+44 20 7212 4555), Tony de Bell (+44 20 7213 5336), Dave Kaplan (+1 973 236 7219) or Brett Cohen (+1 973 236 7201).

Yours faithfully,

*PricewaterhouseCoopers LLP*



## Appendix

### Preliminary Views on Revenue Recognition in Contracts with Customers

#### 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?*

We agree with the boards' proposal for a single revenue recognition principle. We concur with the boards' observation that the guidance in existing literature is industry specific which, at times, can produce different accounting for economically similar transactions. A single principle for revenue recognition will help achieve consistency across transactions and industries.

We also agree that revenue recognition should be based on changes in assets and liabilities. This is more consistent with other literature in the accounting frameworks than the current revenue recognition model, which is based on an earnings approach.

We suggest that the standard include a clear definition of "revenue." We believe this will help distinguish performance obligations that represent revenue generating activities from other liabilities in contracts with customers. It should also help achieve consistency in what is classified as revenue in the performance statement.

#### 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?*

We believe that a single principle for revenue recognition for all transactions would be ideal. We recognise it is difficult to create an all-encompassing principle that would provide the transparency and decision-useful information users require. We considered whether the proposed principle would provide decision-useful information for the three types of contracts listed below. All three are subject to current projects that address the accounting for assets and liabilities and the resulting income statement effect of changes in those assets and liabilities.

- Financial and non-financial instrument contracts that are within the scope of financial instrument accounting guidance. We believe financial instruments should be accounted for in accordance with the guidance developed for the recognition and measurement of such contracts. The proposed revenue model is based on the satisfaction of performance obligations, which are promises to provide goods or services, whereas financial instruments are contracts to pay or receive cash. We agree that application of the proposed model to such contracts may not provide decision-useful information.
- Insurance contracts. We believe it would be more appropriate to address the accounting for insurance contracts within the boards' current project on insurance contracts. Such contracts often have insurance risk, investment, and service elements, and include a conditional requirement to pay cash to the policyholder. Some of these characteristics are similar to the characteristics of financial instruments (i.e., promises to receive and/or pay cash rather than promises to provide goods or services) which makes it unclear how some of the concepts in the discussion paper would be applied.



The boards should, however, ensure that if, or to the extent, they conclude insurance is a service, there is broad consistency between the revenue recognition component of the accounting model developed for insurance contracts and the revenue recognition model in this discussion paper. Economically similar transactions should be accounted for similarly. For example, a warranty is in substance insurance provided to the customer, but warranties are within the scope of the revenue recognition project. We believe the boards should strive to ensure that contracts with similar characteristics are accounted for consistently whether within the scope of the revenue project or the insurance project.

- Lease contracts. The boards' discussion paper, "Leases - Preliminary Views", proposes that revenue recognition for lessors be aligned with the revenue recognition principle proposed in this project. The accounting for revenue from leases, whether they relate to intangible or tangible assets, should be similar irrespective of what standard is applied. It is critical that the boards ensure that the conclusions in these projects are aligned. The boards should also consider whether the revenue standard and the lease standard should have consistent effective dates to minimise the risk of inconsistent guidance.

We believe the above contracts should not be within the scope of this project, but that customer consideration related to these items may be presented as revenue in the performance statement if the definition of revenue is met.

The contracts discussed above may contain performance obligations that would appear to be covered by the proposed revenue standard (e.g., a contract outside the scope of the revenue standard that includes a customer loyalty programme). We believe the boards should clarify, either in the revenue standard or in the projects above, whether such performance obligations should be separated and accounted for under the revenue standard.

We understand the boards will consider the implications of the proposed model for entities that recognise revenue or gains in the absence of a contract. We do not believe it would be appropriate to present changes in the value of assets as revenue absent a contract with a customer. Gains arising on remeasurement of assets (e.g., gains arising on the remeasurement of inventory or investment property) prior to entering into a contract with a customer do not satisfy the revenue recognition principle in the discussion paper. Such gains could be presented as unrealised gains in the performance statement.

### **Question 3**

*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.*

We agree with the boards' proposed definition of a contract. The definition appropriately captures arrangements intended to be within the scope of the guidance. However, we believe the boards should also provide a principle for determining what constitutes the contract (i.e., the unit of account) to reflect the economics of the arrangement between the parties. The principle should require that separate contracts be combined if they are so closely related or economically interdependent that the commercial effect of one contract is best understood in conjunction with the other contract. The principle should also be sufficiently robust to address the accounting for contract options, modifications, renewals, and variations/change orders. We believe existing guidance in both frameworks' construction contract standards provides factors that could be considered in developing such a principle.

The boards' emphasis on the contract makes it important to differentiate between arrangements and contract terms that are substantive and those that lack commercial substance. We do not believe that a revenue standard should be applied to contracts that lack commercial substance. This would include,



for example, non-substantive exchanges of inventory. We also do not believe that a revenue standard should be applied to contract terms that lack commercial substance. This would include artificially segmenting a contract into individual performance obligations that do not reflect the substance of the arrangement.

#### Question 4

*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.*

We agree there should be a single definition that applies to all promises to a customer in a contract. A performance obligation is defined in the discussion paper as "a promise in a contract with a customer to transfer an asset (such as a good or a service) to that customer." We agree with this definition but believe application guidance would help entities identify performance obligations.

The discussion paper refers to performance obligations as enforceable promises in a contract. It discusses explicit and implicit promises, including those created by operation of law and those constructively created by an entity's established practices. It is unclear whether a constructive or implicit performance obligation established other than by law is an enforceable promise. An entity may be economically compelled to perform, but not legally required to do so. We suggest that the boards clarify that a performance obligation includes promises to deliver goods or services that are explicit in the contract, created by law, and created implicitly by established business practices under which a customer has a reasonable expectation of performance.

Correctly defining the performance obligation is critical to assessing when control transfers and revenue is recognised. It would therefore be helpful for the boards to illustrate how the definition of a performance obligation would be applied in practice. For example:

- A statutory obligation, such as a warranty, while not contractual is a promise to deliver services that is enforceable by law and thus is a performance obligation.
- Sales incentives that provide a free or discounted good or service in the future in conjunction with a current transaction are performance obligations.
- Rights to exchange goods are performance obligations.
- Conditional promises, such as when-and-if upgrades, are performance obligations because an entity is contractually obliged to provide such upgrades, if they are developed, to the customer. The fact that the entity is not contractually obliged to develop such upgrades should be considered in determining the stand-alone selling price of the performance obligations.

It would also be helpful if the boards clarify whether other arrangements may create performance obligations, such as:

- Promises in a contract that an entity would have performed irrespective of the contract, such as defending a patent for an entity's proprietary technology.
- Constructive promises that are not legally enforceable but are likely to be performed to fulfil customer expectations or reflect the entity's market strategy (e.g., software repair patches offered by a computer manufacturer to customers).
- A promise not to do something, such as a non-compete agreement.
- Product recalls outside of the normal warranty period.
- Payments to change the terms of a contract (e.g., airline change fees).
- Substantive purchase options that are exercisable at the discretion of the customer.
- Prospective or retrospective volume purchase arrangements.
- A product-liability guarantee (e.g., an implicit or explicit promise that the product will not be injurious).



The boards should also address whether obligations to refund cash (e.g., rebates, cash-settled warranties, or service-level guarantees) are an adjustment to the measurement of the transaction price or a performance obligation. We recognise this distinction may be difficult in certain circumstances so clarity would be helpful.

Lastly, it would be beneficial for the boards to provide application guidance for identifying the performance obligations in a service contract. Consider the following examples:

- A real estate agent has been hired to sell a property for which it will receive a fee upon successful completion of the sale. Is the performance obligation the marketing of the property, which is satisfied over the marketing period, or is it the successful sale of the property, which is only satisfied when the sale completes? Would the answer be different if the agent receives non-refundable payments based on time spent?
- A consultant has been hired to perform a valuation and deliver a valuation report. The consultant is paid non-refundable fees based on time and materials over the term of the contract. Is the performance obligation the delivery of the valuation report or the valuation service being performed over the period? Would the answer change if payment was contingent on delivery of the report? Would the answer change if replacing the consultant meant re-performing the service?
- An outsourcer has agreed to provide payroll services for a fixed fee over five years. The outsourcer will need to perform set-up activities such as transferring data and establishing procedures. Are such set-up activities performance obligations? Would the answer change if these activities were specified in the contract? Would the answer change if the customer specifically paid for these services?

#### 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?*

We agree that performance obligations should be separated when they are transferred to the customer at different times. However, we believe there are a number of other situations where an entity will need to separate performance obligations. An entity that delivers multiple goods and/or services concurrently may need to separate those performance obligations for measurement or disclosure purposes. Separation of each of the performance obligations will be necessary to properly allocate contract consideration under a relative selling price approach if two or more performance obligations are settled concurrently but others settled at different times. A single contract that provides for the concurrent transfer of goods or provision of services may also require separation for income statement presentation and segment disclosures.

#### 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?*

We believe that an entity's obligation to stand ready to accept a returned good is a performance obligation. However, we believe that a conditional obligation to refund cash is a financial liability rather than a performance obligation.

The discussion paper explores two methods for accounting for a customer's right to return a product: as a performance obligation or as a failed sale. Each of these models creates challenges in



application. The performance obligation model explained in the discussion paper suggests that the return of inventory is recorded as if the entity entered into a transaction with the original customer to repurchase inventory at the original sales price. We believe that recording the inventory repurchase in this manner would not reflect the commercial substance of the transaction, because the return is the unwinding of the original sale rather than a separate transaction.

We believe recording the repurchase of inventory at the original sales price creates an inconsistency between the revenue recognised and the cash retained by the entity. It also creates an inconsistency between the amount of inventory derecognised and the amount recorded as cost of sales. Both revenue and cost of sales will be equally overstated when the product is resold. Revenue is overstated because it is recognised twice for the sale of the same goods (assuming they are resold). Cost of sales is overstated because the returned goods were taken back into inventory at original selling price rather than original cost. For these reasons we do not believe that accounting for returns solely as a performance obligation reflects the economics of the transaction or provides decision-useful information.

The boards' description of the failed-sale model results in an entity continuing to recognise goods on its balance sheet despite transferring control of those goods to the customer. This creates an exception to the control transfer principle and fails to recognise the seller's obligation to stand-ready to accept returned goods. We do not believe creating an exception to the principle is appropriate.

We do not believe that the two models are mutually exclusive. The models can be combined to more accurately reflect the commercial substance of the transaction and eliminate any exceptions to the control transfer principle. A transaction with a return right creates a stand-ready performance obligation for the entity to accept returned goods, but the entity should not recognise revenue for those sales expected to fail. Inventory should be derecognised when control transfers to the customer. We believe therefore that the boards should consider a modified failed sale model.

An entity should first determine whether the original sale transaction will result in goods being returned and the consideration repaid (i.e., whether the sale will fail). A failed sale results in the entity receiving cash but recording a liability to return that cash. The entity also retains a right to recover inventory in exchange for the refund of cash. This right to recover the inventory should be recorded at the seller's original cost of the goods to be returned. The right to recover the inventory should be assessed for impairment if evidence suggests a decline in the value of the goods expected to be returned below their original cost.

A stand-ready performance obligation to accept returned goods exists for both successful and failed sales. An entity satisfies this performance obligation over the expected return period, with adjustments to reflect actual returns. We recognise that determining the stand-alone selling price of the stand ready performance obligation may be difficult and, in many cases, the stand-alone selling price of such an obligation may be insignificant.

We believe this model can be applied either to single items or to sales of a large number of homogenous products when an entity can estimate the expected level of failed sales.

#### **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 agree that a sales incentive for a free or discounted product or service in the future that is provided in conjunction with a current transaction gives rise to a performance obligation. A seller that provides a customer with a good or service currently, together with the right to future discounts (such as customer



loyalty points or vouchers for free goods and services) has entered into a contract containing more than one performance obligation. The sales incentives should be accounted for separately from the initial sale as the incentive is a separate performance obligation that is satisfied at a later date.

We believe the accounting for a contract that transfers a good or service together with the right to a free or discounted good or service in the future should be accounted for differently than an incentive that only provides for a return of cash to the customer. The latter situation does not require the delivery of a good or service in the future. Incentives that provide for the return of cash should be considered in measuring the transaction price at the inception of the contract.

Judgment will be required to measure the stand-alone selling price of such incentives. We suggest the boards consider whether the stand-alone selling price should be reduced for discounts generally available to market participants and also consider the potential impact of forfeitures (i.e., "breakage") on the allocation of revenue to individual performance obligations.

### 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 support the boards' conclusion 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. We further agree with the boards' observation that current practice has divergent recognition models: one based on the transfer of risks and rewards and another based on the activities of an entity. Having two divergent models can provide inconsistent answers for economically similar transactions. We believe that a focus on control, in combination with the appropriate identification of performance obligations, will result in more consistent decisions about when assets are transferred and when revenue is recognised.

We acknowledge that recognising revenue based on the notion of control transfer will often require significant judgment. The boards should articulate a clear principle of when control of an asset transfers from an entity to a customer. This principle should be supported by indicators to assist in determining when the principle is met. We offer the boards the following suggestions:

Control transfer principle:

Control has transferred when the customer has the right to direct, use, or access at will the resource underlying the asset (whether a good or a service) so as to enjoy the economic benefits of that asset or preclude or limit its use by others.

Control transfer – indicators:

The indicators suggested below are not intended to be all inclusive nor is any one factor determinative. An entity should assess the specific facts and circumstances of each contract and conclude, based on the preponderance of indicators, whether control has transferred.

- The customer has obtained legal title to the resource underlying the asset (although there may be situations where control of the resource underlying the asset may pass at a different time than legal title).
- The customer has obtained physical possession of the resource underlying the asset; for example, an asset being constructed on the customer's premises.
- The customer has a unilateral ability to sell the resource underlying the asset.



- The customer has the ability to use (or consume immediately) the resource underlying the asset. For example, a customer that has engaged a vendor to provide security services would immediately consume the asset as the services are performed.
- The customer has the ability (whether exercised or not) to make substantive changes to the design of the asset during the contract period.
- The customer has the ability to pledge the asset, for example, as collateral.
- The customer has the ability to restrict access, use or sale of the asset by others, including the vendor.
- The customer has the right to the resource underlying the asset, for example, through lien rights, title transfer or enforceable contract terms. The customer's right to take over work in process suggests that the vendor is, in effect, continuously transferring control of the resource underlying the asset to the customer. Conversely, a vendor's right to require a customer to give back goods may indicate that the vendor controls the resource underlying the asset.
- The customer has custodial risk of loss associated with the asset.
- The customer has obtained physical possession of a tangible asset and the vendor's activities serve only to enhance that physical asset.
- The customer has an obligation to make non-refundable payments for work in process (whether for a tangible or intangible asset or services). Such terms may indicate that transfer of control occurs continuously.

The principle and indicators mirror the term used in the discussion paper, i.e. the "resource underlying the asset." It would be helpful if the boards explain what differences, if any, exist between the "resource underlying the asset" and the asset itself. For example, it is unclear whether there is any difference between the ability to sell or pledge the asset and the ability to sell or pledge the right to buy the completed asset.

The boards should provide clarity on the allocation of consideration between performance obligations when control continuously transfers. For example, paragraphs A34 and A35 appear to provide conflicting guidance on the determination of the performance obligation, which in turn impacts the allocation of consideration.

The boards should also address the measurement of revenue when control of an asset (whether a good or service) continuously transfers. Addressing this within the context of the revenue standard is critical. The boards should consider the extent to which existing guidance under both IFRS and U.S. GAAP for percentage of completion accounting, using either output or input measures, accurately reflects the continuous transfer of control of an asset and should thus be incorporated in the revenue recognition standard.

We believe there are conceptual similarities between the principle underlying the transfer of control in the discussion paper and the principles being discussed in the financial instruments derecognition project. We also note that there are existing standards for derecognition of a liability and encourage the boards to consider the interaction between these existing standards, the financial instruments derecognition project and this proposed model.



#### Question 9

*The boards propose 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.*

We agree that, for those contracts within the scope of the revenue recognition standard, an entity should recognise revenue only when a performance obligation is satisfied.

#### 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.*

- (a) Do you agree that performance obligations should be measured initially at the transaction price? Why or why not?*
  - (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?*
  - (c) 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.*
  - (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.*
- (a) We agree that initial measurement of performance obligations at the transaction price is appropriate. We also agree that there are a number of variables that can impact the transaction price, including time value of money, contingent revenue, uncertainty of collection, non-cash consideration and other adjustments to the consideration (e.g., rebates). Measurement of the contract asset determines the revenue to be allocated to the performance obligations, so a clear principle should be developed for determining the transaction price to ensure the consistency the boards seek in recognising revenue.
- (b) We do not believe that remeasurement of performance obligations when deemed onerous should be addressed in a revenue recognition standard. The recognition of an onerous contract provision is an accrual of costs and not a performance obligation. Guidance on the existence, recognition and measurement of onerous contracts, therefore, should not be addressed by a revenue standard. The boards' tentative conclusion creates an unnecessary exception to the transaction price model and leads to potential complexities (e.g., unit of account, costs to include, etc.). It would also appear to contradict the direction of the boards' conceptual framework projects.
- (c,d) We believe the proposed measurement approach provides decision-useful information for all performance obligations, subject to our comments in Question 2 above regarding the scope of the revenue standard.



#### Question 11

*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 (e.g. selling costs) are included in the initial measurement of the performance obligations. The boards propose that an entity should recognise 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?*

*(b) 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.*

(a) We believe an entity should allocate the transaction price to the performance obligations at contract inception. This principle should be consistently applied irrespective of whether an entity explicitly charges a customer to recover the costs of obtaining a contract. We also agree that costs should be recorded as expenses unless such costs qualify for recognition as an asset in accordance with other standards, though some enhancement to those other standards may be needed.

While some guidance currently exists in both frameworks on capitalisation of costs, more detailed guidance may be needed for some situations such as long-term construction or service contracts. Consequential amendments may be needed to the existing asset standards to provide sufficient guidance on the treatment of contract related costs so that decision-useful information reflecting the economics of the transaction is provided.

We note that more extensive changes to the asset guidance may be needed under U.S. GAAP due to the lack of a single standard addressing the capitalisation of property, plant and equipment and the fragmented guidance for other assets (e.g., inventory and intangible assets). There may also be insufficient guidance in the U.S. standards once capitalisation guidance currently included in industry specific revenue recognition literature no longer exists.

(b) There may be some situations where contract origination costs meet the definition of an asset. There are a number of industries, such as insurance, investment management, and telecommunications, where significant amounts are paid to third parties to obtain a contract with a customer and the related cash flow stream. We believe the boards should consider whether there is sufficient guidance in the relevant asset standards to enable an entity to determine when the costs associated with the acquisition of these cash flow streams should result in the recognition of an asset. We do not believe such guidance should be included within the revenue standard.

#### 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?*

We agree that stand-alone selling prices of goods or services underlying performance obligations should form the basis for allocating the transaction price. Entities should be capable of separating a transaction into performance obligations and estimating stand-alone selling prices even if the items are not sold separately by the entity. The relative stand-alone selling price approach provides the most



reasonable basis for the allocation of transaction price once stand-alone selling prices are derived or estimated.

The boards should consider whether multiple performance obligations to deliver identical products have the same estimated stand-alone selling price. For example, an entity may enter into a contract to deliver 1000 widgets and, as a result of efficiencies and other market-place factors, the average price of 1000 widgets may be different than the price of a single widget.

#### **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 stand-alone selling price of a good or service should be capable of being measured in most circumstances, even if the entity does not sell the good or service separately. The estimate of stand-alone selling price should form the basis for allocation of the transaction price. Please refer to our response to Question 12 above.

We acknowledge that in some circumstances it may be difficult to estimate the stand-alone selling price of an asset such as unique intellectual property rights. It would be helpful for the boards to provide application guidance in such circumstances. Robust disclosure should also be required in these cases.