AASB Exposure Draft

Tier 2 Supplement to ED 198
November 2010

Revenue from Contracts with Customers

Comments to AASB by 31 January 2011

Australian Government

Australian Accounting Standards Board

Commenting on this Tier 2 Supplement to AASB Exposure Draft

Comments on this Tier 2 Supplement to AASB Exposure Draft ED 198 are requested by 31 January 2011. Comments should be addressed to:

The Chairman
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All submissions on possible, proposed or existing financial reporting requirements, or on the standard-setting process, will be placed on the public record unless the Chairman of the AASB agrees to those submissions being treated as confidential. The latter will only occur if the public interest warrants such treatment.

Obtaining a Copy of this Tier 2 Supplement to AASB Exposure Draft

This Tier 2 Supplement to AASB Exposure Draft ED 198 is available on the AASB website: www.aasb.gov.au. Alternatively, printed copies of this Supplement are available by contacting:

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AASB REQUEST FOR COMMENTS

Reduced Disclosure Requirements

AASB 1053 *Application of Tiers of Australian Accounting Standards* establishes a differential reporting framework consisting of two tiers of reporting requirements for preparing general purpose financial statements:

(a) Tier 1: Australian Accounting Standards; and

(b) Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements (RDR).

Tier 2 comprises the recognition, measurement and presentation requirements of Tier 1 and substantially reduced disclosures corresponding to those requirements.

This Tier 2 Supplement to AASB Exposure Draft ED 198 *Revenue from Contracts with Customers* sets out the disclosures proposed in ED 198 (which incorporates International Accounting Standards Board [IASB] ED/2010/6 *Revenue from Contracts with Customers*) and analyses whether they should be included in Tier 2 reporting requirements. The proposals should not be seen as any indication of AASB support or otherwise for the IASB's proposed disclosures in ED/2010/6. That will be determined through the ED 198 due process.

Due Date for Comments to the AASB

Comments on this Tier 2 Supplement to ED 198 should be submitted to the AASB by 31 January 2011.

AASB Specific Matters for Comment

The AASB would particularly value comments on the following:

1. whether you agree with the AASB disclosure proposals under Tier 2 as set out in the attached analysis;

2. whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:

   (a) not-for-profit entities; and

   (b) public sector entities;

3. whether, overall, the proposals would result in financial statements that would be useful to users;

4. whether the proposals are in the best interests of the Australian economy; and

5. unless already provided in response to specific matters for comment 1 – 4 above, the costs and benefits of the proposals, whether quantitative (financial or non-financial) or qualitative.

Submissions play an important role in the decisions that the AASB will make in regard to a Standard. The AASB would prefer that respondents supplement their opinions with detailed comments, whether supportive or critical, on the major issues. The AASB regards both critical and supportive comments as essential to a balanced review and will consider all submissions, whether they address all specific matters, additional issues or only one issue.

ANALYSIS OF PROPOSED DISCLOSURES

The purpose of this Tier 2 Supplement to ED 198 is to propose whether Tier 2 entities should be exempted from making certain disclosures proposed in ED 198 in their general purpose financial statements.

Determining Tier 2 Disclosure

In determining the proposed reduced disclosure requirements, consideration has been given to the principles that were applied in analysing full International Financial Reporting Standards (IFRSs) as adopted in Australia when the reduced disclosure requirements were first established for Tier 2 entities. The principles for determining Tier 2 disclosure requirements ('Tier 2 Disclosure Principles') are as follows:

(a) drawing directly on the *International Financial Reporting Standard for Small and Medium-Sized Entities (IFRS for SMEs)* when the Tier 2 recognition and measurement requirements are the same as those under the *IFRS for SMEs*; and

(b) using the 'user need' and 'cost-benefit' principles applied by the IASB in developing its *IFRS for SMEs* when the Tier 2 recognition and measurement requirements are not the same as those available under the *IFRS for SMEs*.

Further explanation of the above principles is provided on the AASB website[1]. Because the distinction between principles (a) and (b) above is dependent on whether there are differences in recognition and measurement requirements under Tier 2 and the *IFRS for SMEs*, the differences pertinent to this exposure draft are identified below.

Comparison of ED 198 and Section 23 of *IFRS for SMEs*

Section 23 of the *IFRS for SMEs* deals with the accounting for revenue for certain transactions and events. ED 198 deals with the accounting for revenue from contracts with customers with some exceptions. The scope difference between ED 198 and the *IFRS for SMEs* arises from the requirement in ED 198 for the existence of a contract with the customer.

The disclosures proposed in ED 198 and the disclosure requirements in Section 23 *Revenue* of the *IFRS for SMEs* have been compared. There are differences between ED 198 and Section 23 in terms of the recognition and measurement requirements.

Recognition, Measurement and Presentation Requirements

Section 23 of the *IFRS for SMEs* differs from ED 198 with respect to the recognition of revenue in a number of ways, including the following.

(a) The *IFRS for SMEs* has different recognition requirements for the following categories of revenue: sale of goods, rendering of services, construction contracts and interest, royalties and dividends. The revenue recognition proposals of ED 198 are applied consistently based on the existence of a contract.

(b) The recognition requirements of the *IFRS for SMEs* are largely based on the transfer of significant risks and rewards (sale of goods) and when it is probable that economic benefits associated with the transaction will flow to the entity. The recognition proposals of ED 198 are based on the satisfaction of performance obligations by the transfer of a promised good or service (when control passes to the customer).

1 See www.aasb.gov.au/Work-In-Progress/Reduced-Disclosure-Requirements/Tier-2-Disclosure-Principles.aspx.

Section 23 of the *IFRS for SMEs* differs from ED 198 with respect to the measurement of revenue in a number of ways, including the following.

(a) The *IFRS for SMEs* measures revenue at the fair value of the consideration received or receivable with an adjustment for deferred payments. ED 198 proposes measuring revenue at an amount which reflects the probability-weighted amount of consideration expected to be received.

(b) The amount of revenue that would be recognised under ED 198 is affected by the following elements: collectibility, time value of money, non-cash consideration and consideration payable to the customer, which are in addition to the measurement requirements of the *IFRS for SMEs*.

Tier 2 Disclosure Proposals

It is proposed to exempt Tier 2 entities from the proposed disclosure requirements in paragraphs 73(b), 75, 76, 80 and 82(b) and the reference to IFRS 8 *Operating Segments* in paragraph 72.

An analysis of the proposed disclosure requirements is available on the AASB website[2]. The full text of the proposed reduced disclosure requirements, with shading to identify the proposed exemptions for Tier 2 entities, is provided below.

2 See www.aasb.gov.au/Work-In-Progress/Reduced-Disclosure-Requirements/Analyses-of-Disclosure-Requirements.aspx.

Proposed Reduced Disclosure Requirements

The following are the disclosure requirements proposed in ED 198 *Revenue from Contracts with Customers* (June 2010), showing requirements from which it is proposed entities applying Tier 2 requirements should be exempt as shaded text.

69 To help users of financial statements understand the amount, timing and uncertainty of revenue and cash flows arising from contracts with customers, an entity shall disclose qualitative and quantitative information about:

- **(a) its contracts with customers (paragraphs 73–80[ψ]); and**
- **(b) the significant judgements, and changes in judgements, made in applying the [draft] IFRS to those contracts (paragraphs 81–83[ψ]).**

70 An entity shall consider the level of detail necessary to satisfy the disclosure requirements and how much emphasis to place on each of the various requirements. An entity shall aggregate or disaggregate disclosures so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items that have different characteristics.

71 If the disclosures provided in accordance with this [draft] IFRS and other IFRSs do not meet the objective in paragraph 69, an entity shall disclose whatever additional information is necessary to meet that objective.

72 Other IFRSs (for example, IFRS 8 *Operating Segments*) require an entity to present and disclose information related to revenue. The entity need not disclose information in accordance with this [draft] IFRS if it has provided the information in accordance with another IFRS. However, an entity shall present and disclose the additional information in accordance with this [draft] IFRS in a way that shows how it relates to information required by that other IFRS.

Contracts with customers

73 An entity shall disclose information about its contracts with customers to help users understand the amount, timing and uncertainty of revenue and cash flows from those contracts, including:

- (a) a disaggregation of revenue for the period (paragraph 74);
- (b) a reconciliation from the opening to the closing aggregate balance of contract assets and contract liabilities (paragraphs 75 and 76); and
- (c) information about the entity's performance obligations (paragraphs 77 and 78), including additional information about its onerous performance obligations (paragraphs 79 and 80).

Disaggregation of revenue

74 An entity shall disaggregate revenue into the categories that best depict how the amount, timing and uncertainty of revenue and cash flows are affected by economic factors. Examples of categories that might be appropriate include:

- (a) type of good or service (for example, major product lines);
- (b) geography (for example, country or region);
- (c) market or type of customer (for example, government versus non-government customers); or
- (d) type of contract (for example, a fixed-price versus a time-and-materials contract).

Reconciliation of contract balances

75 An entity shall provide a reconciliation from the opening to the closing aggregate balance of contract assets and contract liabilities. The reconciliation shall, at a minimum, show each of the following, if applicable:

- (a) the amount(s) recognised in the statement of comprehensive income arising from:
  - (i) revenue from performance obligations satisfied during the reporting period;

(ψ) RDR footnote: Where there is a cross reference to a disclosure requirement in this Standard that is shaded for Tier 2 entities, the cross reference should be treated as shaded accordingly.

(ii) revenue from allocating changes in the transaction price to performance obligations satisfied in previous reporting periods;
(iii) interest income and expense; and
(iv) the effect of changes in foreign exchange rates;

(b) cash received;
(c) amounts transferred to receivables;
(d) non-cash consideration received; and
(e) contracts acquired in business combinations and contracts disposed.

76 An entity shall reconcile the opening and closing aggregate balance of contract assets and contract liabilities to the amounts presented in the statement of financial position.

Performance obligations

77 An entity shall disclose information about its performance obligations in contracts with customers, including a description of:
(a) the goods or services the entity has promised to transfer, highlighting any performance obligations to arrange for another party to transfer goods or services (ie if the entity is acting as an agent);
(b) when the entity typically satisfies its performance obligations (for example, upon shipment, upon delivery, as services are rendered or upon completion of service);
(c) the significant payment terms (for example, whether the consideration amount is variable and whether the contract has a material financing component);
(d) obligations for returns, refunds and other similar obligations; and
(e) types of warranties and related obligations.

78 For contracts with an original expected duration of more than one year, an entity shall disclose the amount of the transaction price allocated to the performance obligations remaining at the end of the reporting period that are expected to be satisfied in each of the following periods:
(a) not later than one year;
(b) later than one year but not later than two years;
(c) later than two years but not later than three years; and
(d) later than three years.

Onerous performance obligations

79 An entity shall disclose the amount of any liability recognised for onerous performance obligations together with a discussion of:
(a) the nature and amount of the performance obligations for which the liability has been recognised;
(b) why those performance obligations have become onerous; and
(c) when the entity expects to satisfy the liability.

80 An entity shall provide a reconciliation from the opening to the closing balance of the liability recognised for onerous performance obligations. The reconciliation shall show the amounts recognised in the statement of comprehensive income attributable to each of the following, if applicable:
(a) performance obligations that became onerous during the period;
(b) performance obligations that ceased to be onerous during the period;
(c) amount of the liability that was satisfied during the period;
(d) the time value of money; and
(e) changes in the measurement of the liability that occurred during the reporting period.

Significant judgements in the application of the [draft] IFRS

81 An entity shall disclose the judgements, and changes in judgements, made in applying this [draft] IFRS that significantly affect the determination of the amount and timing of revenue from contracts with customers. That disclosure shall explain the judgements used in:

(a) determining the timing of satisfaction of performance obligations (paragraph 82[Ψ]); and
(b) determining the transaction price and allocating it to performance obligations (paragraph 83).

Determining the timing of satisfaction of performance obligations

82 For performance obligations satisfied continuously, an entity shall disclose:
(a) the methods (for example, output methods, input methods and methods based on the passage of time) used to recognise revenue; and
(b) an explanation of why such methods are a faithful depiction of the transfer of goods or services.

Determining the transaction price and allocating it to performance obligations

83 An entity shall disclose information about the methods, inputs and assumptions used:
(a) to determine the transaction price in accordance with paragraphs 35–49;
(b) to estimate stand-alone selling prices of promised goods or services;
(c) to measure obligations for returns, refunds and other similar obligations;
(d) to measure the amount of any liability recognised for onerous performance obligations (including information about the discount rate).