AASB Exposure Draft

ED 267
August 2015

Clarifications to AASB 15

Comments to the AASB by 2 October 2015

Australian Government

Australian Accounting Standards Board

How to comment on this AASB Exposure Draft

Constituents are strongly encouraged to respond to the AASB and the IASB. The AASB is seeking comment by 2 October 2015. This will enable the AASB to consider Australian constituents' comments in the process of formulating its own comments to the IASB, which are due by 28 October 2015.

Formal submissions

Submissions should be lodged online via the "Work in Progress – Open for Comment" page of the AASB website (www.aasb.gov.au/comment) as a PDF document and, if possible, a Word document (for internal use only).

Other feedback

Other feedback is welcomed and may be provided via the following methods:

E-mail: standard@aasb.gov.au
Phone: (03) 9617 7600

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 Chair of the AASB agrees to submissions being treated as confidential. The latter will occur only if the public interest warrants such treatment.

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AASB REQUEST FOR COMMENTS

The Australian Accounting Standards Board's (AASB's) policy is to incorporate International Financial Reporting Standards (IFRSs) into Australian Accounting Standards. Accordingly, the AASB is inviting comments on:

(a) any of the proposals in the attached International Accounting Standards Board (IASB) Exposure Draft, including the specific questions on the proposals as listed in the Invitation to Comment section of the attached IASB Exposure Draft; and

(b) the 'AASB Specific Matters for Comment' listed below.

AASB Specific Matters for Comment

The AASB would particularly value comments on the following:

1. 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, including GAAP/GFS implications;

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

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

4. unless already provided in response to specific matters for comment 1 – 3 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative. In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the proposals relative to the existing requirements.

July 2015

Exposure Draft ED/2015/6

Clarifications to IFRS 15

Comments to be received by 28 October 2015

IASB®

IFRS®

Clarifications to IFRS 15

Comments to be received by 28 October 2015

Exposure Draft ED/2015/6 *Clarifications to IFRS 15* is published by the International Accounting Standards Board (IASB) for comment only. The proposals may be modified in the light of the comments received before being issued in final form. Comments need to be received by **28 October 2015** and should be submitted in writing to the address below or electronically using our ‘Comment on a proposal’ page.

All comments will be on the public record and posted on our website unless the respondent requests confidentiality. Such requests will not normally be granted unless supported by good reason, for example, commercial confidence. Please see our website for details on this and how we use your personal data.

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Introduction

In May 2014, the International Accounting Standards Board (IASB) and the US national standard-setter, the Financial Accounting Standards Board (FASB), jointly issued a new revenue Standard—IFRS 15 *Revenue from Contracts with Customers* and Topic 606 *Revenue from Contracts with Customers*. After issuing the new revenue Standard, the IASB and the FASB (collectively, the 'Boards') formed the Transition Resource Group (TRG) for Revenue Recognition to support implementation of the Standard. One of the objectives of the TRG is to inform the Boards about implementation issues which would help the Boards determine what, if any, action should be undertaken to address those issues. Information about the objectives, composition and operating procedures of the TRG is available on the IASB's website at go.ifrs.org/RTRG.

Since its formation, the TRG has met five times to discuss submissions from stakeholders regarding the implementation of the new revenue Standard. The TRG meets in public and the agenda papers, recordings of the meetings and meeting reports that summarise the issues discussed as well as the next steps are available on the IASB website at go.ifrs.org/RTRG-meetings.

The substantial majority of the issues discussed by the TRG have been resolved without standard setting. However, the TRG's discussions on five topics indicated potential differences of views on how to implement the requirements in the new revenue Standard. Consequently, those topics were identified as requiring consideration by the Boards. Those topics were:

(a) identifying performance obligations;

(b) principal versus agent considerations;

(c) licensing;

(d) collectability; and

(e) measuring non-cash consideration.

Additionally, the Boards received requests from some stakeholders for practical expedients in respect of the following:

(a) accounting for modifications to a contract that occurred before transition to the new revenue Standard;

(b) for entities electing to use the full retrospective transition method, accounting for a contract completed under previous revenue Standards before transition to the new revenue Standard; and

(c) assessing whether a sales tax (or a similar tax) is collected on behalf of a third party.

The Boards discussed the five topics and the possible practical expedients and decided to propose targeted amendments to the new revenue Standard. The IASB decided to propose clarifications with respect to identifying performance obligations, principal versus agent considerations and licensing. The IASB concluded that it was not necessary to amend IFRS 15 with respect to collectability or measuring non-cash consideration. In respect of the practical expedients, the IASB decided to propose transition relief for modified contracts and completed contracts.

The FASB decided to propose more extensive amendments to Topic 606 to clarify the requirements on all five topics. The FASB also decided to propose similar transition relief for modified contracts and, instead of applying the requirements in Topic 606, an option to present all sales taxes on a net basis. The FASB decided not to propose transition relief for completed contracts.

In reaching its conclusions to propose clarifying amendments and transition relief to IFRS 15, the IASB considered the need to balance being responsive to issues raised to help entities implement IFRS 15 but, at the same time, not creating a level of uncertainty about the Standard to the extent that the IASB's actions might be disruptive to the implementation process. The IASB noted that, when new Standards are issued, there are always initial questions that arise. Those questions are generally resolved as entities, auditors and others work through them over time, and gain a better understanding of the new requirements. The IASB also considered the effect of any differences between its decisions and those made by the FASB. With these wider considerations in mind, the IASB considered whether, and how best, to clarify particular requirements in IFRS 15 at this time.

Because of the different decisions made, the IASB and the FASB are each publishing separate Exposure Drafts. In May 2015, the FASB published *Proposed Accounting Standards Update: Identifying Performance Obligations and Licensing*. The FASB is expected to publish further Proposed Accounting Standard Update(s) later in 2015 relating to its proposed clarifications on principal versus agent considerations, collectability, measuring non-cash consideration and practical expedients relating to transition and the presentation of sales taxes. Although in some cases both Boards have decided to propose clarifications to the same topics, the wording of the proposed clarifications is not (or is not expected to be) the same with the exception of the proposals regarding principal versus agent considerations. The Basis for Conclusions on this Exposure Draft notes when the IASB has identified circumstances in which differences in outcomes may arise as a consequence of the different decisions reached by both Boards.

The IASB is of the view that the application of judgement is a necessary and desirable aspect of representing faithfully an entity's revenue generating transactions. Accordingly, the proposed clarifications are not intended to remove the need for judgement when applying IFRS 15. Rather, they are intended to clarify the principles and the guidance in the Standard to assist in the consistent application of judgement.

Next steps

The IASB intends to consider the comments it receives on these proposals and decide whether to proceed with amendments to IFRS 15. The IASB expects to complete its redeliberations by the end of 2015.

Although it is possible that further implementation issues could arise, the IASB expects that any further issues are unlikely to lead to standard setting before it undertakes the post-implementation review of IFRS 15. This is because entities, auditors and others have had fourteen months since the issuance of the new revenue Standard to identify implementation issues—the IASB expects any substantive implementation issues to have been identified in that time period. In addition, recognising that any further changes to IFRS 15 could disrupt, rather than help, the implementation process, the IASB is reluctant to propose any further amendments until after the post implementation review.

Invitation to comment

The IASB invites comments on the proposals in this Exposure Draft, particularly on the questions set out below. Comments are most helpful if they:

(a) comment on the questions as stated;

(b) indicate the specific paragraph(s) to which they relate;

(c) contain a clear rationale; and

(d) describe any alternative that the IASB should consider, if applicable.

The IASB is not requesting comments on matters in IFRS 15 that are not addressed in this Exposure Draft.

Comments should be submitted in writing so as to be received no later than **28 October 2015**.

Questions for respondents

Question 1—Identifying performance obligations
IFRS 15 requires an entity to assess the goods or services promised in a contract to identify the performance obligations in that contract. An entity is required to identify performance obligations on the basis of promised goods or services that are distinct. To clarify the application of the concept of 'distinct', the IASB is proposing to amend the Illustrative Examples accompanying IFRS 15. In order to achieve the same objective of clarifying when promised goods or services are distinct, the FASB has proposed to clarify the requirements of the new revenue Standard and add illustrations regarding the identification of performance obligations. The FASB's proposals include amendments relating to promised goods or services that are immaterial in the context of a contract, and an accounting policy election relating to shipping and handling activities that the IASB is not proposing to address. The reasons for the IASB's decisions are explained in paragraphs BC7–BC25. Do you agree with the proposed amendments to the Illustrative Examples accompanying IFRS 15 relating to identifying performance obligations? Why or why not? If not, what alternative clarification, if any, would you propose and why?

Question 2—Principal versus agent considerations
When another party is involved in providing goods or services to a customer, IFRS 15 requires an entity to determine whether it is the principal in the transaction or the agent. To do so, an entity assesses whether it controls the specified goods or services before they are transferred to the customer. To clarify the application of the control principle, the IASB is proposing to amend paragraphs B34–B38 of IFRS 15, amend Examples 45–48 accompanying IFRS 15 and add Examples 46A and 48A. The FASB has reached the same decisions as the IASB regarding the application of the control principle when assessing whether an entity is a principal or an agent, and is expected to propose amendments to Topic 606 that are the same as (or similar to) those included in this Exposure Draft in this respect. The reasons for the Boards' decisions are explained in paragraphs BC26–BC56. Do you agree with the proposed amendments to IFRS 15 regarding principal versus agent considerations? In particular, do you agree that the proposed amendments to each of the indicators in paragraph B37 are helpful and do not raise new implementation questions? Why or why not? If not, what alternative clarification, if any, would you propose and why?

Question 3—Licensing
When an entity grants a licence to a customer that is distinct from other promised goods or services, IFRS 15 requires the entity to determine whether the licence transfers to a customer either at a point in time (providing the right to use the entity's intellectual property) or over time (providing the right to access the entity's intellectual property). That determination largely depends on whether the contract requires, or the customer reasonably expects, the entity to undertake activities that significantly affect the intellectual property to which the customer has rights. IFRS 15 also includes requirements relating to sales-based or usage-based royalties promised in exchange for a licence (the royalties constraint). To clarify when an entity's activities significantly affect the intellectual property to which the customer has rights, the IASB is proposing to add paragraph B59A and delete paragraph B57 of IFRS 15, and amend Examples 54 and 56–61 accompanying IFRS 15. The IASB is also proposing to add paragraphs B63A and B63B to clarify the application of the royalties constraint. The reasons for the IASB's decisions are explained in paragraphs BC57–BC86. The FASB has proposed more extensive amendments to the licensing guidance and the accompanying Illustrations, including proposing an alternative approach for determining the nature of an entity's promise in granting a licence. Do you agree with the proposed amendments to IFRS 15 regarding licensing? Why or why not? If not, what alternative clarification, if any, would you propose and why?

Question 4—Practical expedients on transition
The IASB is proposing the following two additional practical expedients on transition to IFRS 15: (a) to permit an entity to use hindsight in (i) identifying the satisfied and unsatisfied performance obligations in a contract that has been modified before the beginning of the earliest period presented; and (ii) determining the transaction price. (b) to permit an entity electing to use the full retrospective method not to apply IFRS 15 retrospectively to completed contracts (as defined in paragraph C2) at the beginning of the earliest period presented. The reasons for the IASB's decisions are explained in paragraphs BC109–BC115. The FASB is also expected to propose a practical expedient on transition for modified contracts. Do you agree with the proposed amendments to the transition requirements of IFRS 15? Why or why not? If not, what alternative, if any, would you propose and why?

Question 5—Other topics
The FASB is expected to propose amendments to the new revenue Standard with respect to collectability, measuring non-cash consideration and the presentation of sales taxes. The IASB decided not to propose amendments to IFRS 15 with respect to those topics. The reasons for the IASB's decisions are explained in paragraphs BC87–BC108. Do you agree that amendments to IFRS 15 are not required on those topics? Why or why not? If not, what amendment would you propose and why? If you would propose to amend IFRS 15, please provide information to explain why the requirements of IFRS 15 are not clear.

How to comment

Comments should be submitted using one of the following methods.

Electronically (our preferred method)	Visit the 'Comment on a proposal page', which can be found at: go.ifrs.org/comment
Email	Email comments can be sent to: commentletters@ifrs.org
Postal	IFRS Foundation 30 Cannon Street London EC4M 6XH United Kingdom

All comments will be on the public record and posted on our website unless confidentiality is requested. Such requests will not normally be granted unless supported by good reason, for example, commercial confidence. Please see our website for details on this and how we use your personal data.

[Draft] Amendments to IFRS 15 *Revenue from Contracts with Customers*

Paragraphs 22–30 have not been amended but have been included for ease of reference.

Identifying performance obligations

22 **At contract inception, an entity shall assess the goods or services promised in a contract with a customer and shall identify as a performance obligation each promise to transfer to the customer either:**

(a) a good or service (or a bundle of goods or services) that is distinct; or

(b) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer (see paragraph 23).

23 A series of distinct goods or services has the same pattern of transfer to the customer if both of the following criteria are met:

(a) each distinct good or service in the series that the entity promises to transfer to the customer would meet the criteria in paragraph 35 to be a performance obligation satisfied over time; and

(b) in accordance with paragraphs 39–40, the same method would be used to measure the entity's progress towards complete satisfaction of the performance obligation to transfer each distinct good or service in the series to the customer.

Promises in contracts with customers

24 A contract with a customer generally explicitly states the goods or services that an entity promises to transfer to a customer. However, the performance obligations identified in a contract with a customer may not be limited to the goods or services that are explicitly stated in that contract. This is because a contract with a customer may also include promises that are implied by an entity's customary business practices, published policies or specific statements if, at the time of entering into the contract, those promises create a valid expectation of the customer that the entity will transfer a good or service to the customer.

25 Performance obligations do not include activities that an entity must undertake to fulfil a contract unless those activities transfer a good or service to a customer. For example, a services provider may need to perform various administrative tasks to set up a contract. The performance of those tasks does not transfer a service to the customer as the tasks are performed. Therefore, those setup activities are not a performance obligation.

Distinct goods or services

26 Depending on the contract, promised goods or services may include, but are not limited to, the following:

(a) sale of goods produced by an entity (for example, inventory of a manufacturer);

(b) resale of goods purchased by an entity (for example, merchandise of a retailer);

(c) resale of rights to goods or services purchased by an entity (for example, a ticket resold by an entity acting as a principal, as described in paragraphs B34–B38);

(d) performing a contractually agreed-upon task (or tasks) for a customer;

(e) providing a service of standing ready to provide goods or services (for example, unspecified updates to software that are provided on a when-and-if-available basis) or of making goods or services available for a customer to use as and when the customer decides;

(f) providing a service of arranging for another party to transfer goods or services to a customer (for example, acting as an agent of another party, as described in paragraphs B34–B38);

(g) granting rights to goods or services to be provided in the future that a customer can resell or provide to its customer (for example, an entity selling a product to a retailer promises to transfer an additional good or service to an individual who purchases the product from the retailer);

(h) constructing, manufacturing or developing an asset on behalf of a customer;

(i) granting licences (see paragraphs B52–B63); and

(j) granting options to purchase additional goods or services (when those options provide a customer with a material right, as described in paragraphs B39–B43).

27 A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

28 A customer can benefit from a good or service in accordance with paragraph 27(a) if the good or service could be used, consumed, sold for an amount that is greater than scrap value or otherwise held in a way that generates economic benefits. For some goods or services, a customer may be able to benefit from a good or service on its own. For other goods or services, a customer may be able to benefit from the good or service only in conjunction with other readily available resources. A readily available resource is a good or service that is sold separately (by the entity or another entity) or a resource that the customer has already obtained from the entity (including goods or services that the entity will have already transferred to the customer under the contract)

or from other transactions or events. Various factors may provide evidence that the customer can benefit from a good or service either on its own or in conjunction with other readily available resources. For example, the fact that the entity regularly sells a good or service separately would indicate that a customer can benefit from the good or service on its own or with other readily available resources.

29 Factors that indicate that an entity's promise to transfer a good or service to a customer is separately identifiable (in accordance with paragraph 27(b)) include, but are not limited to, the following:

(a) the entity does not provide a significant service of integrating the good or service with other goods or services promised in the contract into a bundle of goods or services that represent the combined output for which the customer has contracted. In other words, the entity is not using the good or service as an input to produce or deliver the combined output specified by the customer.

(b) the good or service does not significantly modify or customise another good or service promised in the contract.

(c) the good or service is not highly dependent on, or highly interrelated with, other goods or services promised in the contract. For example, the fact that a customer could decide to not purchase the good or service without significantly affecting the other promised goods or services in the contract might indicate that the good or service is not highly dependent on, or highly interrelated with, those other promised goods or services.

30 If a promised good or service is not distinct, an entity shall combine that good or service with other promised goods or services until it identifies a bundle of goods or services that is distinct. In some cases, that would result in the entity accounting for all the goods or services promised in a contract as a single performance obligation.

In Appendix B, paragraphs B34–B38 and B58 are amended and paragraphs B34A, B35A, B35B, B37A, B59A, B63A and B63B are added. Paragraph B57 is deleted. Deleted text is struck through and new text is underlined. Paragraphs B52–B56 and B59–B63 have not been amended but have been included for ease of reference.

Principal versus agent considerations

B34 When another party is involved in providing goods or services to a customer, the entity shall determine whether the nature of its promise is a performance obligation to provide the specified goods or services itself (ie the entity is a principal) or to arrange for <u>those goods or services to be provided by</u> the other party ~~to provide those goods or services~~ (ie the entity is an agent). <u>An entity determines whether it is a principal or an agent for each specified good or service promised to the customer. A specified good or service is a distinct good or service (or a distinct bundle of goods or services) to be provided to the customer (see paragraphs 27–30). If a contract with a customer includes more</u>

than one specified good or service, an entity could be a principal for some specified goods or services and an agent for others.

B34A To determine the nature of its promise (as described in paragraph B34), the entity shall:

(a) identify the specified goods or services to be provided to the customer (which, for example, could be a right to a good or service to be provided by another party (see paragraph 26)).

(b) assess whether it controls (as described in paragraph 33) each specified good or service before that good or service is transferred to the customer.

B35 An entity is a principal if ~~the entity~~ it controls ~~a promised~~ the specified good or service before ~~the entity transfers the~~ that good or service is transferred to a customer. However, an entity ~~is~~ does not necessarily ~~acting as a principal~~ control a specified good if the entity obtains legal title of ~~a product~~ that good only momentarily before legal title is transferred to a customer. An entity that is a principal in a contract may satisfy a performance obligation by itself or it may engage another party (for example, a subcontractor) to satisfy some or all of a performance obligation on its behalf.

B35A When another party is involved in providing goods or services to a customer, an entity that is a principal obtains control of:

(a) a good or another asset from the other party that it then transfers to the customer;

(b) a right to a service to be performed by the other party, which gives the entity the ability to direct that party to provide the service to the customer on the entity's behalf; or

(c) a good or service from the other party that it then combines with other goods or services in providing the specified good or service to the customer. If an entity provides a significant service of integrating goods or services provided by another party into the specified good or service for which the customer has contracted, it controls the specified good or service before that good or service is transferred to the customer. In that case, the entity first obtains control of the good or service from the other party and directs its use to create the combined output that is the specified good or service.

B35B When (or as) an entity that is a principal satisfies a performance obligation, the entity recognises revenue in the gross amount of consideration to which it expects to be entitled in exchange for ~~those~~ the specified good~~s~~ or service~~s~~ transferred.

B36 An entity is an agent if the entity's performance obligation is to arrange for the provision of the specified good~~s~~ or service~~s~~ by another party. An entity that is an agent does not control the specified good or service provided by another party before that good or service is transferred to the customer. When (or as) an entity that is an agent satisfies a performance obligation, the entity recognises revenue in the amount of any fee or commission to which it expects to be entitled in exchange for arranging for ~~the other party to provide its~~ the specified goods or services to be provided by the other party. An entity's fee or commission might be the net amount of consideration that the entity retains after paying the other party the consideration received in exchange for the goods or services to be provided by that party.

B37 Indicators that an entity ~~is an agent (and therefore does not~~ controls the specified good or service before it is ~~provided~~ transferred to ~~a~~ the customer~~)~~ include, but are not limited to, the following:

(a) ~~another party~~ the entity is primarily responsible for fulfilling the ~~contract;~~ promise to provide the specified good or service. This typically includes responsibility for the acceptability of the specified good or service. If the entity is primarily responsible for fulfilling the promise to provide the specified good or service, this may indicate that the other party involved in providing the specified good or service is acting on the entity's behalf.

(b) the entity ~~does not have~~ has inventory risk before ~~or after the goods~~ the specified good or service ~~have~~ has been ~~ordered by~~ transferred to a customer~~, during shipping~~ or after that transfer (for example, on return)~~;~~. For example, if the entity obtains, or commits to obtain, the specified good or service before obtaining a contract with the customer, that may indicate that the entity has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the good or service before it is transferred to the customer.

(c) the entity ~~does not have~~ has discretion in establishing prices for the ~~other party's goods or services and, therefore, the benefit that the entity can receive from those goods or services is limited;~~ specified good or service. Establishing the price that the customer pays for the specified good or service may indicate that the entity has the ability to direct the use of that good or service. However, an agent can have discretion in establishing prices in some cases. For example, an agent may have some flexibility in setting prices in order to generate additional revenue from its service of arranging for goods or services to be provided by other parties to customers.

~~(d)~~ ~~the entity's consideration is in the form of a commission; and~~

~~(e)~~(d) the entity is ~~not~~ exposed to credit risk for the amount receivable from ~~a~~ the customer in exchange for the ~~other party's~~ specified good~~s~~ or service~~s~~. For example, if the entity is required to pay the other party involved in providing the specified good or service regardless of whether it obtains payment from the customer, this may indicate that the entity is directing the other party to provide goods or services on the entity's behalf. However, in some cases, an agent may choose to accept credit risk as part of its overall service of arranging for the provision of the specified good or service.

B37A The indicators in paragraph B37 may be more or less relevant to the assessment of control depending on the nature of the specified good or service and the terms and conditions of the contract. In addition, different indicators may provide more persuasive evidence in different contracts.

B38 If another entity assumes the entity's performance obligations and contractual rights in the contract so that the entity is no longer obliged to satisfy the performance obligation to transfer the ~~promised~~ specified good or service to the customer (ie the entity is no longer acting as the principal), the entity shall not recognise revenue for that performance obligation. Instead, the entity shall evaluate whether to recognise revenue for satisfying a performance obligation to obtain a contract for the other party (ie whether the entity is acting as an agent).

...

Licensing

B52 A licence establishes a customer's rights to the intellectual property of an entity. Licences of intellectual property may include, but are not limited to, any of the following:

(a) software and technology;

(b) motion pictures, music and other forms of media and entertainment;

(c) franchises; and

(d) patents, trademarks and copyrights.

B53 In addition to a promise to grant a licence to a customer, an entity may also promise to transfer other goods or services to the customer. Those promises may be explicitly stated in the contract or implied by an entity's customary business practices, published policies or specific statements (see paragraph 24). As with other types of contracts, when a contract with a customer includes a promise to grant a licence in addition to other promised goods or services, an entity applies paragraphs 22–30 to identify each of the performance obligations in the contract.

B54 If the promise to grant a licence is not distinct from other promised goods or services in the contract in accordance with paragraphs 26–30, an entity shall account for the promise to grant a licence and those other promised goods or services together as a single performance obligation. Examples of licences that are not distinct from other goods or services promised in the contract include the following:

(a) a licence that forms a component of a tangible good and that is integral to the functionality of the good; and

(b) a licence that the customer can benefit from only in conjunction with a related service (such as an online service provided by the entity that enables, by granting a licence, the customer to access content).

B55 If the licence is not distinct, an entity shall apply paragraphs 31–38 to determine whether the performance obligation (which includes the promised licence) is a performance obligation that is satisfied over time or satisfied at a point in time.

B56 If the promise to grant the licence is distinct from the other promised goods or services in the contract and, therefore, the promise to grant the licence is a separate performance obligation, an entity shall determine whether the licence transfers to a customer either at a point in time or over time. In making this determination, an entity shall consider whether the nature of the entity's promise in granting the licence to a customer is to provide the customer with either:

(a) a right to access the entity's intellectual property as it exists throughout the licence period; or

(b) a right to use the entity's intellectual property as it exists at the point in time at which the licence is granted.

Determining the nature of the entity's promise

B57 ~~To determine whether an entity's promise to grant a licence provides a customer with either a right to access an entity's intellectual property or a right to use an entity's intellectual property, an entity shall consider whether a customer can direct the use of, and obtain substantially all of the remaining benefits from, a licence at the point in time at which the licence is granted. A customer cannot direct the use of, and obtain substantially all of the remaining benefits from, a licence at the point in time at which the licence is granted if the intellectual property to which the customer has rights changes throughout the licence period. The intellectual property will change (and thus affect the entity's assessment of when the customer controls the licence) when the entity continues to be involved with its intellectual property and the entity undertakes activities that significantly affect the intellectual property to which the customer has rights. In these cases, the licence provides the customer with a right to access the entity's intellectual property (see paragraph B58). In contrast, a customer can direct the use of, and obtain substantially all of the remaining benefits from, the licence at the point in time at which the licence is granted if the intellectual property to which the customer has rights will not change (see paragraph B61). In those cases, any activities undertaken by the entity merely change its own asset (ie the underlying intellectual property), which may affect the entity's ability to provide future licences; however, those activities would not affect the determination of what the licence provides or what the customer controls.~~ [Deleted]

B58 The nature of an entity's promise in granting a licence is a promise to provide a right to access the entity's intellectual property if all of the following criteria are met:

(a) the contract requires, or the customer reasonably expects, that the entity will undertake activities that significantly affect the intellectual property to which the customer has rights (see paragraphs B59–B59A);

(b) the rights granted by the licence directly expose the customer to any positive or negative effects of the entity's activities identified in paragraph B58(a); and

(c) those activities do not result in the transfer of a good or a service to the customer as those activities occur (see paragraph 25).

B59 Factors that may indicate that a customer could reasonably expect that an entity will undertake activities that significantly affect the intellectual property include the entity's customary business practices, published policies or specific statements. Although not determinative, the existence of a shared economic interest (for example, a sales-based royalty) between the entity and the customer related to the intellectual property to which the customer has rights may also indicate that the customer could reasonably expect that the entity will undertake such activities.

B59A An entity's activities significantly affect the intellectual property when either:

(a) those activities are expected to change the form (for example, the design) or the functionality (for example, the ability to perform a function or task) of the intellectual property to which the customer has rights; or

(b) the ability of the customer to obtain benefit from the intellectual property to which the customer has rights is substantially derived from, or dependent upon, those activities. For example, the benefit from a brand is often derived from, or dependent upon, the entity's ongoing activities that support or maintain the value of the intellectual property.

Accordingly, if the intellectual property to which the customer has rights has significant stand-alone functionality, a substantial portion of the benefit of that intellectual property is derived from that functionality. Therefore, that intellectual property would not be significantly affected by the entity's activities unless those activities change that functionality.

B60 If the criteria in paragraph B58 are met, an entity shall account for the promise to grant a licence as a performance obligation satisfied over time because the customer will simultaneously receive and consume the benefit from the entity's performance of providing access to its intellectual property as the performance occurs (see paragraph 35(a)). An entity shall apply paragraphs 39–45 to select an appropriate method to measure its progress towards complete satisfaction of that performance obligation to provide access.

B61 If the criteria in paragraph B58 are not met, the nature of an entity's promise is to provide a right to use the entity's intellectual property as that intellectual property exists (in terms of form and functionality) at the point in time at which the licence is granted to the customer. This means that the customer can direct the use of, and obtain substantially all of the remaining benefits from, the licence at the point in time at which the licence transfers. An entity shall account for the promise to provide a right to use the entity's intellectual property as a performance obligation satisfied at a point in time. An entity shall apply paragraph 38 to determine the point in time at which the licence transfers to the customer. However, revenue cannot be recognised for a licence that provides a right to use the entity's intellectual property before the beginning of the period during which the customer is able to use and benefit from the licence. For example, if a software licence period begins before an entity provides (or otherwise makes available) to the customer a code that enables the customer to immediately use the software, the entity would not recognise revenue before that code has been provided (or otherwise made available).

B62 An entity shall disregard the following factors when determining whether a licence provides a right to access the entity's intellectual property or a right to use the entity's intellectual property:

(a) Restrictions of time, geographical region or use—those restrictions define the attributes of the promised licence, rather than define whether the entity satisfies its performance obligation at a point in time or over time.

(b) Guarantees provided by the entity that it has a valid patent to intellectual property and that it will defend that patent from unauthorised use—a promise to defend a patent right is not a performance obligation because the act of defending a patent protects the value of the entity's intellectual property assets and provides assurance to the customer that the licence transferred meets the specifications of the licence promised in the contract.

Sales-based or usage-based royalties

B63 Notwithstanding the requirements in paragraphs 56–59, an entity shall recognise revenue for a sales-based or usage-based royalty promised in exchange for a licence of intellectual property only when (or as) the later of the following events occurs:

(a) the subsequent sale or usage occurs; and

(b) the performance obligation to which some or all of the sales-based or usage-based royalty has been allocated has been satisfied (or partially satisfied).

B63A The requirement on sales-based or usage-based royalties in paragraph B63 applies when the royalty relates only to a licence of intellectual property or when a licence of intellectual property is the predominant item to which the royalty relates.

B63B Revenue from a sales-based or usage-based royalty should be recognised entirely in accordance with either the requirement in paragraph B63 (if paragraph B63 applies) or the requirements on variable consideration in paragraphs 50–59 (if paragraph B63 does not apply).

In Appendix C, paragraphs C2 and C5 are amended and paragraphs C1A, C7A and C8A are added. Deleted text is struck through and new text is underlined. Paragraphs C3 and C6 have not been amended but have been included for ease of reference.

Effective date

...

C1A [Draft] *Clarifications to IFRS 15*, issued in [date], amended paragraphs B34–B38, B58, C2 and C5, deleted paragraph B57 and added paragraphs B34A, B35A, B35B, B37A, B59A, B63A, B63B, C7A and C8A. An entity shall apply those amendments for annual reporting periods beginning on or after [date]. Earlier application is permitted. If an entity applies those amendments for an earlier period, it shall disclose that fact.

Transition

C2 For the purposes of the transition requirements in paragraphs C3–C8A:

(a) the date of initial application is the start of the reporting period in which an entity first applies this Standard; and

(b) a completed contract is a contract for which the entity has transferred all of the goods or services identified in accordance with IAS 11 *Construction Contracts*, IAS 18 *Revenue* and related Interpretations.

C3 An entity shall apply this Standard using one of the following two methods:

(a) retrospectively to each prior reporting period presented in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, subject to the expedients in paragraph C5; or

(b) retrospectively with the cumulative effect of initially applying this Standard recognised at the date of initial application in accordance with paragraphs C7–C8.

...

C5 An entity may use one or more of the following practical expedients when applying this Standard retrospectively in accordance with paragraph C3(a):

(a) for completed contracts, an entity need not restate contracts that:

(i) begin and end within the same annual reporting period; or

(ii) are completed contracts at the beginning of the earliest period presented.

(b) for completed contracts that have variable consideration, an entity may use the transaction price at the date the contract was completed rather than estimating variable consideration amounts in the comparative reporting periods~~; and~~.

(c) for contracts that were modified before the beginning of the earliest period presented, an entity need not retrospectively restate the contract for those contract modifications in accordance with paragraphs 20–21. Instead, an entity shall reflect the aggregate effect of all of the modifications that occur before the beginning of the earliest period presented when:

(i) identifying the satisfied and unsatisfied performance obligations; and

(ii) determining the transaction price.

~~(c)~~(d) for all reporting periods presented before the date of initial application, an entity need not disclose the amount of the transaction price allocated to the remaining performance obligations and an explanation of when the entity expects to recognise that amount as revenue (see paragraph 120).

C6 For any of the practical expedients in paragraph C5 that an entity uses, the entity shall apply that expedient consistently to all contracts within all reporting periods presented. In addition, the entity shall disclose all of the following information:

(a) the expedients that have been used; and

(b) to the extent reasonably possible, a qualitative assessment of the estimated effect of applying each of those expedients.

...

C7A An entity may also use the practical expedient described in paragraph C5(c) when applying this Standard retrospectively in accordance with paragraph C3(b). If an entity uses this practical expedient, the entity shall apply the expedient consistently to all contracts and disclose the information required by paragraph C6.

...

C8A An entity shall apply [Draft] *Clarifications to IFRS 15* (see paragraph C1A) retrospectively in accordance with IAS 8. In applying the amendments retrospectively, an entity shall apply the amendments as if they had been included in IFRS 15 at the date of initial application. As a consequence, an entity does not apply the amendments to reporting periods or contracts to which the requirements of IFRS 15 are not applied in accordance with paragraphs C2–C8. For example, if an entity applies the transition method in paragraph C3(b), the entity does not restate contracts that are completed at the date of initial application for the effects of these amendments.

[Draft] Amendments to the Illustrative Examples on IFRS 15 *Revenue from Contracts with Customers*

Paragraphs IE51, IE61, IE232, IE237–IE238, IE241–IE243, IE247–IE248, IE277, IE279, IE286–IE287, IE290–IE291, IE294, IE296, IE299–IE300, IE305, IE307, IE308, IE310–IE311 and IE313 are amended. Paragraphs IE48A–IE48D and their related headings, IE58A–IE58L and their related headings, IE232A–IE232C, IE237A–IE237B, IE238A–IE238G and their related heading, IE242A–IE242C, IE247A–IE247B, and IE248A–IE248F and their related heading are added. Deleted text is struck through and new text is underlined. Other paragraphs that have not been amended have been included for ease of reference.

Example 10—Goods and services are not distinct

Case A—Significant integration service (single item)

IE45 An entity, a contractor, enters into a contract to build a hospital for a customer. The entity is responsible for the overall management of the project and identifies various goods and services to be provided, including engineering, site clearance, foundation, procurement, construction of the structure, piping and wiring, installation of equipment and finishing.

IE46 The promised goods and services are capable of being distinct in accordance with paragraph 27(a) of IFRS 15. That is, the customer can benefit from the goods and services either on their own or together with other readily available resources. This is evidenced by the fact that the entity, or competitors of the entity, regularly sells many of these goods and services separately to other customers. In addition, the customer could generate economic benefit from the individual goods and services by using, consuming, selling or holding those goods or services.

IE47 However, the goods and services are not distinct within the context of the contract in accordance with paragraph 27(b) of IFRS 15 (on the basis of the factors in paragraph 29 of IFRS 15). That is, the entity's promise to transfer individual goods and services in the contract are not separately identifiable from other promises in the contract. This is evidenced by the fact that the entity provides a significant service of integrating the goods and services (the inputs) into the hospital (the combined output) for which the customer has contracted.

IE48 Because both criteria in paragraph 27 of IFRS 15 are not met, the goods and services are not distinct. The entity accounts for all of the goods and services in the contract as a single performance obligation.

Case B—Significant integration service (multiple items)

IE48A An entity enters into a contract with a customer to produce multiple units of a highly complex, specialised device. The specifications are unique to the customer based on a custom design that was developed under the terms of a separate contract. The entity is responsible for the overall management of the contract, which requires the integration of various activities including procuring materials, identifying and managing subcontractors, and performing manufacturing, assembly, and testing of the devices.

IE48B The promised goods and services are capable of being distinct in accordance with paragraph 27(a) of IFRS 15. That is, the customer can benefit from the goods and services either on their own or together with other readily available resources. This is evidenced by the fact that the entity, or competitors of the entity, regularly sells many of these goods and services separately to other customers. The entity also observes that each device can function independently of the other devices.

IE48C The entity also considers the factors in paragraph 29 of IFRS 15 and determines that its promises to transfer the individual goods and services in the contract are not separately identifiable (thus the criterion in paragraph 27(b) of IFRS 15 is not met). This is because the entity is responsible for the overall management of the contract and for integrating various goods and services (the inputs) to produce the full complement of devices (the combined output) for which the customer has contracted. The entity's performance obligation is the overall production of the units, including establishing a production process solely for the purpose of producing units in accordance with the agreed upon specifications of this contract.

IE48D Because both criteria in paragraph 27 of IFRS 15 are not met, the goods and services are not distinct. The entity accounts for all of the goods and services promised in the contract as a single performance obligation.

Example 11—Determining whether goods or services are distinct

Case A—Distinct goods or services

IE49 An entity, a software developer, enters into a contract with a customer to transfer a software licence, perform an installation service and provide unspecified software updates and technical support (online and telephone) for a two-year period. The entity sells the licence, installation service and technical support separately. The installation service includes changing the web screen for each type of user (for example, marketing, inventory management and information technology). The installation service is routinely performed by other entities and does not significantly modify the software. The software remains functional without the updates and the technical support.

IE50 The entity assesses the goods and services promised to the customer to determine which goods and services are distinct in accordance with paragraph 27 of IFRS 15. The entity observes that the software is delivered before the other goods and services and remains functional without the updates and the technical support. Thus, the entity concludes that the customer can benefit from each of the goods and services either on their own or together with the other goods and services that are readily available and the criterion in paragraph 27(a) of IFRS 15 is met.

IE51 The entity also considers the factors in paragraph 29 of IFRS 15 and determines that the promise to transfer each good and service to the customer is separately identifiable from each of the other promises (thus the criterion in paragraph 27(b) of IFRS 15 is met). In particular, the entity observes that, although it integrates the software into the customer's system, the installation service does not significantly modify or customise the software itself and, as such, the software and the installation service are separate outputs promised by the entity instead of inputs used to produce a combined output. Even though the installation service, the software updates and the technical support depend on the transfer of the licence, the entity could fulfil its promise to transfer the software licence, and the customer could benefit from the licence, independently of these promises. Similarly, the customer could acquire the software licence separately without significantly affecting the entity's promises to provide the installation services, software updates or technical support. Accordingly, the promises are not highly dependent on, or interrelated with, each other.

IE52 On the basis of this assessment, the entity identifies four performance obligations in the contract for the following goods or services:

(a) the software licence;

(b) an installation service;

(c) software updates; and

(d) technical support.

IE53 The entity applies paragraphs 31–38 of IFRS 15 to determine whether each of the performance obligations for the installation service, software updates and technical support are satisfied at a point in time or over time. The entity also assesses the nature of the entity's promise to transfer the software licence in accordance with paragraph B58 of IFRS 15 (see Example 54 in paragraphs IE276–IE277).

Case B—Significant customisation

IE54 The promised goods and services are the same as in Case A, except that the contract specifies that, as part of the installation service, the software is to be substantially customised to add significant new functionality to enable the software to interface with other customised software applications used by the customer. The customised installation service can be provided by other entities.

IE55 The entity assesses the goods and services promised to the customer to determine which goods and services are distinct in accordance with paragraph 27 of IFRS 15. The entity observes that the terms of the contract result in a promise to provide a significant service of integrating the licenced software into the existing software system by performing a customised installation service as specified in the contract. In other words, the entity is using the licence and the customised installation service as inputs to produce the combined output (ie a functional and integrated software system) specified in the contract (see paragraph 29(a) of IFRS 15). In addition, the software is significantly modified and customised by the service (see paragraph 29(b) of IFRS 15). Although the customised installation service can be provided by other entities, the entity determines that within the context of the contract, the promise to transfer the licence is not separately identifiable from the customised installation service and, therefore, the criterion in paragraph 27(b) of IFRS 15 (on the basis of the factors in paragraph 29 of IFRS 15) is not met. Thus, the software licence and the customised installation service are not distinct.

IE56 As in Case A, the entity concludes that the software updates and technical support are distinct from the other promises in the contract. This is because the customer can benefit from the updates and technical support either on their own or together with the other goods and services that are readily available and because the promise to transfer the software updates and the technical support to the customer are separately identifiable from each of the other promises.

IE57 On the basis of this assessment, the entity identifies three performance obligations in the contract for the following goods or services:

(a) customised installation service (that includes the software licence);

(b) software updates; and

(c) technical support.

IE58 The entity applies paragraphs 31–38 of IFRS 15 to determine whether each performance obligation is satisfied at a point in time or over time.

Case C—Promises are separately identifiable (installation)

IE58A An entity enters into a contract with a customer to provide an item of equipment as well as to provide installation services. The equipment is functional without any customisation or modification and the installation required is capable of being performed by other service providers.

IE58B The entity assesses the goods and services promised to the customer to determine which goods or services are distinct in accordance with paragraph 27 of IFRS 15. The entity observes that the customer can benefit from the equipment on its own, by using it or reselling it for an amount greater than scrap value and can benefit from the installation services together with a resource (the equipment) that it has already obtained from the entity. Thus, the entity concludes that the criterion in paragraph 27(a) of IFRS 15 is met, and both the equipment and installation services are capable of being distinct.

IE58C The entity also considers the factors in paragraph 29 of IFRS 15 and determines that its promises to transfer the equipment and to provide the installation services are separately identifiable (thus the criterion in paragraph 27(b) of IFRS 15 is met). The entity observes that the installation will not significantly modify or customise the equipment, and fulfilling its promises in the contract does not require a significant integration service. The entity has promised to deliver the equipment and then install it; it has not promised to combine the equipment and the installation services in a way that would transform them into a different, combined output. Even though the installation depends on the successful transfer of the equipment to the customer, the entity could fulfil its promise to deliver the equipment without having to install it. Similarly, the entity could fulfil the installation service if the customer had acquired the equipment from another entity. Accordingly, the entity's promise to deliver the equipment and its promise to provide installation services are not highly dependent on, or interrelated with, each other.

IE58D On the basis of this assessment, the entity identifies two performance obligations in the contract for the following goods or services:

(a) the equipment; and

(b) installation services.

IE58E The entity applies paragraphs 31–38 of IFRS 15 to determine whether each performance obligation is satisfied at a point in time or over time.

Case D—Promises are separately identifiable (contractual restrictions)

IE58F Assume the same facts as in Case C, except that the customer is contractually required to use the entity's installation services.

IE58G The contractual requirement to use the entity's installation services would not change the entity's conclusion that its promises to transfer the equipment and to provide the installation services are distinct in accordance with paragraph 27 of IFRS 15. This is because the contractual requirement to use the entity's installation services does not change the characteristics of the goods or services themselves, nor does it change the entity's promises to the customer. Although the customer is required to use the entity's installation services, they are still capable of being distinct and the entity's promise to provide the equipment and its promise to provide the installation services are separately identifiable.

Case E—Promises are separately identifiable (consumables)

IE58H An entity enters into a contract with a customer to provide an item of off-the-shelf equipment (ie it is functional without any significant customisation or modification) and to provide specialised consumables for use in the equipment at predetermined intervals over the next three years. The consumables are produced only by the entity, but are sold separately by the entity.

IE58I The entity determines that the customer can benefit from the equipment together with other readily available resources (ie consumables it could obtain from the entity), and that the customer can benefit from the consumables that will be provided under the contract together with the delivered equipment. Therefore, the entity concludes that the equipment and the consumables are each capable of being distinct in accordance with paragraph 27(a) of IFRS 15.

IE58J The entity determines that its promises to transfer the equipment and to provide consumables over a three-year period are each separately identifiable in accordance with paragraph 27(b) of IFRS 15. The entity observes that it has not promised to provide a significant integration service that transforms the equipment and consumables into a different, combined output, and the equipment and consumables are not significantly customised or modified from the form in which each is sold separately. Although the consumables are required for the machine to function, the entity can satisfy its promise to deliver the equipment independently of its promise to deliver the consumables. If the customer decided not to purchase the consumables, it would not significantly affect the entity's promise to transfer the equipment to the customer. Similarly, if the customer separately acquired the equipment, it would not significantly affect the entity's promise to provide the consumables. Accordingly, the entity's promise to provide the equipment and its promise to provide specialised consumables are not highly dependent on, or interrelated with, each other.

IE58K On the basis of this assessment, the entity identifies two performance obligations in the contract for the following goods or services:

(a) the equipment; and

(b) the consumables.

IE58L The entity applies paragraphs 31–38 of IFRS 15 to determine whether each performance obligation is satisfied at a point in time or over time.

Example 12—Explicit and implicit promises in a contract

IE59 An entity, a manufacturer, sells a product to a distributor (ie its customer) who will then resell it to an end customer.

Case A—Explicit promise of service

IE60 In the contract with the distributor, the entity promises to provide maintenance services for no additional consideration (ie ‘free’) to any party (ie the end customer) that purchases the product from the distributor. The entity outsources the performance of the maintenance services to the distributor and pays the distributor an agreed-upon amount for providing those services on the entity’s behalf. If the end customer does not use the maintenance services, the entity is not obliged to pay the distributor.

IE61 Because the promise of maintenance services is a promise to transfer goods or services in the future and is part of the negotiated exchange between the entity and the distributor, the entity determines that the promise to provide maintenance services is a ~~performance obligation~~ promised good or service (see paragraph 26(g) of IFRS 15). The entity concludes that the promise would represent a performance obligation regardless of whether the entity, the distributor, or a third party provides the service. Consequently, the entity allocates a portion of the transaction price to the promise to provide maintenance services.

...

Example 45—Arranging for the provision of goods or services (entity is an agent)

IE231 An entity operates a website that enables customers to purchase goods from a range of suppliers who deliver the goods directly to the customers. When a good is purchased via the website, the entity is entitled to a commission that is equal to 10 per cent of the sales price. The entity’s website facilitates payment between the supplier and the customer at prices that are set by the supplier. The entity requires payment from customers before orders are processed and all orders are non-refundable. The entity has no further obligations to the customer after arranging for the products to be provided to the customer.

IE232 To determine whether the entity’s performance obligation is to provide the specified goods itself (ie the entity is a principal) or to arrange for the supplier to provide those goods (ie the entity is an agent), the entity ~~considers~~ identifies the ~~nature of its promise~~ specified good or service to be provided to the customer and assesses whether it controls that good or service before the good or service is transferred to the customer. ~~Specifically, the entity observes that the supplier of~~

~~the goods delivers its goods directly to the customer and thus the entity does not obtain control of the goods. Instead, the entity's promise is to arrange for the supplier to provide those goods to the customer.~~

IE232A The website operated by the entity is a marketplace in which suppliers offer their goods and customers purchase the goods that are offered. Accordingly, the entity observes that the specified goods to be provided to customers that use the website are the goods provided by the suppliers, and no other promises are made to customers by the entity.

IE232B The entity concludes that it does not control the specified goods before they are transferred to customers that order goods using the website. The entity does not at any time have the ability to direct the use of the goods transferred to customers. For example, it cannot direct the goods to parties other than the customers or prevent the supplier from transferring those goods to the customers. The entity does not control the suppliers' inventory of goods used to fulfil the orders placed by customers using the website.

IE232C ~~In~~ As part of reaching that conclusion, the entity considers the following indicators ~~from~~ in paragraph B37 of IFRS 15 ~~as follows~~. The entity concludes that these indicators provide further evidence that it does not control the specified goods before they are transferred to the customers:

(a) the supplier is primarily responsible for fulfilling the ~~contract—ie by shipping the goods to the customer;~~ promise to provide the goods to the customer. The entity is neither obliged to provide the goods if the supplier fails to transfer the goods to the customer, nor responsible for the acceptability of the goods.

(b) the entity does not take inventory risk at any time ~~during the transaction because the goods are shipped directly by the supplier~~ before or after the goods are transferred to the customer~~;~~. The entity does not commit to obtain the goods from the supplier before the goods are purchased by the customer, and does not accept responsibility for any damaged or returned goods.

~~(c)~~ ~~the entity's consideration is in the form of a commission (10 per cent of the sales price);~~

~~(d)~~(c) the entity does not have discretion in establishing prices for the supplier's goods ~~and, therefore, the benefit the entity can receive from those goods is limited; and~~. The sales price is set by the supplier.

~~(e)~~ ~~neither the entity, nor the supplier, has credit risk because payments from customers are made in advance.~~

IE233 Consequently, the entity concludes that it is an agent and its performance obligation is to arrange for the provision of goods by the supplier. When the entity satisfies its promise to arrange for the goods to be provided by the supplier to the customer (which, in this example, is when goods are purchased by the customer), the entity recognises revenue in the amount of the commission to which it is entitled.

Example 46—Promise to provide goods or services (entity is a principal)

IE234 An entity enters into a contract with a customer for equipment with unique specifications. The entity and the customer develop the specifications for the equipment, which the entity communicates to a supplier that the entity contracts with to manufacture the equipment. The entity also arranges to have the supplier deliver the equipment directly to the customer. Upon delivery of the equipment to the customer, the terms of the contract require the entity to pay the supplier the price agreed to by the entity and the supplier for manufacturing the equipment.

IE235 The entity and the customer negotiate the selling price, and the entity invoices the customer for the agreed-upon price with 30-day payment terms. The entity's profit is based on the difference between the sales price negotiated with the customer and the price charged by the supplier.

IE236 The contract between the entity and the customer requires the customer to seek remedies for defects in the equipment from the supplier under the supplier's warranty. However, the entity is responsible for any corrections to the equipment required resulting from errors in specifications.

IE237 To determine whether the entity's performance obligation is to provide the specified goods or services itself (ie the entity is a principal) or to arrange for ~~another party to provide~~ those goods or services to be provided by another party (ie the entity is an agent), the entity ~~considers the nature of its promise~~ identifies the specified good or service to be provided to the customer and assesses whether it controls that good or service before the good or service is transferred to the customer. ~~The entity has promised to provide the customer with specialised equipment; however, the entity has subcontracted the manufacturing of the equipment to the supplier. In determining whether the entity obtains control of the equipment before control transfers to the customer and whether the entity is a principal, the entity considers the indicators in paragraph B37 of IFRS 15 as follows:~~

~~(a)~~ ~~the entity is primarily responsible for fulfilling the contract. Although the entity subcontracted the manufacturing, the entity is ultimately responsible for ensuring that the equipment meets the specifications for which the customer has contracted.~~

~~(b)~~ ~~the entity has inventory risk because of its responsibility for corrections to the equipment resulting from errors in specifications, even though the supplier has inventory risk during production and before shipment.~~

~~(c)~~ ~~the entity has discretion in establishing the selling price with the customer, and the profit earned by the entity is an amount that is equal to the difference between the selling price negotiated with the customer and the amount to be paid to the supplier.~~

~~(d)~~ ~~the entity's consideration is not in the form of a commission.~~

~~(e)~~ ~~the entity has credit risk for the amount receivable from the customer in exchange for the equipment.~~

IE237A The entity concludes that it has promised to provide the customer with specialised equipment. Although the entity has subcontracted the manufacturing of the equipment to the supplier, the entity concludes that the development of the specifications and the manufacturing of the equipment are not distinct because they are not separately identifiable (ie there is a single performance obligation). The entity is responsible for the overall management of the contract and, thus, provides a significant service of integrating those items into the combined output—the specialised equipment—for which the customer has contracted. In addition, these activities are highly interrelated; for example, if necessary modifications to the specifications are identified as the equipment is manufactured, the entity is responsible for communicating revisions to the supplier and for ensuring that any associated rework required conforms with the revised specifications. Accordingly, the entity identifies the specified good to be provided to the customer as the specialised equipment.

IE237B The entity concludes that it controls the specialised equipment before that equipment is transferred to the customer in accordance with paragraph B35A(c). The entity provides the significant integration service necessary to produce the specialised equipment and, therefore, controls the specialised equipment before it is transferred to the customer. The entity directs the use of the supplier's manufacturing service in creating the combined output that is the specialised equipment. In reaching the conclusion that it controls the specialised equipment before it is transferred to the customer, the entity also observes that, even though the supplier delivers the specialised equipment to the customer, the supplier has no ability to direct its use (ie the supplier cannot decide to use the specialised equipment for another purpose or direct that equipment to another customer). The terms of the entity's contract with the supplier prevent the supplier from directing the use of the specialised equipment by specifying that the equipment must be delivered to the customer. The entity also obtains the remaining benefits from the specialised equipment by being entitled to the consideration in the contract from the customer.

IE238 ~~The entity concludes that its promise is to provide the equipment to the customer. On the basis of the indicators in paragraph B37 of IFRS 15, the entity concludes that it controls the equipment before it is transferred to the customer.~~ Thus, the entity concludes that it is a principal in the transaction ~~and~~. The entity does not consider the indicators in paragraph B37 of IFRS 15 because the evaluation above is conclusive without consideration of the indicators. The entity recognises revenue in the gross amount of consideration to which it is entitled from the customer in exchange for the specialised equipment.

Example 46A—Promise to provide goods or services (entity is a principal)

IE238A An entity enters into a contract with a customer to provide office maintenance services. The entity and the customer define and agree the scope of the services and negotiate the price. The entity is responsible for ensuring that the services are performed in accordance with the terms and conditions in the contract. The entity invoices the customer for the agreed-upon price on a monthly basis with 10-day payment terms.

IE238B The entity regularly engages third-party service providers to provide office maintenance services to its customers. When the entity obtains a contract from a customer, the entity in turn enters into a contract with one of those service providers directing the service provider to perform office maintenance services for the customer. The payment terms in the contracts with the service providers are generally aligned with the payment terms in the entity's contracts with customers. However, the entity is obliged to pay the service provider even if the customer fails to pay for any reason.

IE238C To determine whether the entity is a principal or an agent, the entity identifies the specified good or service to be provided to the customer and assesses whether it controls that good or service before the good or service is transferred to the customer.

IE238D The entity observes that the specified services to be provided to the customer are the office maintenance services, and that no other promises are made to the customer.

IE238E The entity concludes that it obtains control of the right to those services (which will be performed by the service provider) before those services are provided to the customer. The terms of the entity's contract with the service provider give the entity the ability to direct the service provider to provide the specified services on the entity's behalf. In addition, the entity concludes that the following indicators in paragraph B37 of IFRS 15 provide further evidence that the entity controls the office maintenance services before they are provided to the customer:

(a) the entity is primarily responsible for fulfilling the promise to provide office maintenance services. Although the entity has subcontracted the services to the service provider, the entity is responsible for the acceptability of the services (ie the entity is responsible for fulfilment of the promise in the contract, regardless of whether the entity performs the services itself or engages a third-party service provider to perform the services).

(b) the entity has discretion in setting the price for the services to the customer.

(c) the entity has credit risk for the amount receivable from the customer in exchange for the office maintenance services. The entity is required to pay the service provider regardless of whether it obtains payment from the customer.

IE238F The entity observes that it does not commit to obtain the services from the service provider before obtaining the contract with the customer, nor does it maintain available resources to provide maintenance services (for example, staff, equipment, or supplies). Thus, the entity does not have inventory risk with respect to the office maintenance services. Nonetheless, the entity concludes that it controls the office maintenance services before they are provided to the customer based on the evidence in paragraph IE238E.

IE238G Thus, the entity is a principal in the transaction and recognises revenue in the amount of consideration to which it is entitled from the customer in exchange for the office maintenance services.

Example 47—Promise to provide goods or services (entity is a principal)

IE239 An entity negotiates with major airlines to purchase tickets at reduced rates compared with the price of tickets sold directly by the airlines to the public. The entity agrees to buy a specific number of tickets and must pay for those tickets regardless of whether it is able to resell them. The reduced rate paid by the entity for each ticket purchased is negotiated and agreed in advance.

IE240 The entity determines the prices at which the airline tickets will be sold to its customers. The entity sells the tickets and collects the consideration from customers when the tickets are purchased; therefore there is no credit risk.

IE241 The entity also assists the customers in resolving complaints with the service provided by the airlines. However, each airline is responsible for fulfilling obligations associated with the ticket, including remedies to a customer for dissatisfaction with the service.

IE242 To determine whether the entity's performance obligation is to provide the specified goods or services itself (ie the entity is a principal) or to arrange for ~~another party to provide~~ those goods or services to be provided by another party (ie the entity is an agent), the entity ~~considers the nature of its promise~~ identifies the specified good or service to be provided to the customer and assesses whether it controls that good or service before the good or service is transferred to the customer.

IE242A The entity concludes that, with each ticket that it commits to purchase from the airline, it obtains control of a right to fly on a specified flight (in the form of a ticket) that the entity then transfers to its customers. Consequently, the entity determines that ~~its promise is to provide the customer with a ticket, which provides the right to fly on the specified flight or another flight if the specified flight is changed or cancelled~~ the specified good or service to be provided to the customer is that right the entity controls. The entity observes that no other promises are made to the customer. ~~In determining whether the entity obtains control of the right to fly before control transfers to the customer and whether the entity is a principal, the entity considers the indicators in paragraph B37 of IFRS 15 as follows:~~

~~(a)~~ ~~the entity is primarily responsible for fulfilling the contract, which is providing the right to fly. However, the entity is not responsible for providing the flight itself, which will be provided by the airline.~~

~~(b)~~ ~~the entity has inventory risk for the tickets because they are purchased before they are sold to the entity's customers and the entity is exposed to any loss as a result of not being able to sell the tickets for more than the entity's cost.~~

~~(c)~~ ~~the entity has discretion in setting the sales prices for tickets to its customers.~~

~~(d) as a result of the entity's ability to set the sales prices, the amount that the entity earns is not in the form of a commission, but instead depends on the sales price it sets and the costs of the tickets that were negotiated with the airline.~~

IE242B The entity controls the right to each flight before it transfers that right to one of its customers because the entity has the ability to direct the use of those rights by deciding whether to use the tickets to fulfil contracts with customers and, if so, which contracts they will fulfil. The entity also has the ability to obtain the remaining benefits from those rights by either reselling the tickets and obtaining all of the proceeds from those sales or, alternatively, using the tickets itself.

IE242C Indicators (b) and (c) in paragraph B37 of IFRS 15 also provide evidence that the entity controls the right to each flight before that right is transferred to the customer. The entity has inventory risk with respect to the tickets because the entity committed to obtain the tickets from the airlines before obtaining a contract with a customer to purchase the tickets. Accordingly, the entity is obliged to pay the airlines for those rights regardless of whether it is able to obtain customers to whom to resell those tickets or whether it can obtain a favourable price for those tickets. The entity also establishes the price that its customers will pay for the tickets.

IE243 ~~The entity concludes that its promise is to provide a ticket (ie a right to fly) to the customer. On the basis of the indicators in paragraph B37 of IFRS 15, the entity concludes that it controls the ticket before it is transferred to the customer.~~ Thus, the entity concludes that it is a principal in the transactions with customers ~~and~~. The entity recognises revenue in the gross amount of consideration to which it is entitled in exchange for the tickets transferred to the customers.

Example 48—Arranging for the provision of goods or services (entity is an agent)

IE244 An entity sells vouchers that entitle customers to future meals at specified restaurants. These vouchers are sold by the entity and the sales price of the voucher provides the customer with a significant discount when compared with the normal selling prices of the meals (for example, a customer pays CU100 for a voucher that entitles the customer to a meal at a restaurant that would otherwise cost CU200). The entity does not purchase vouchers in advance; instead, it purchases vouchers only as they are requested by the customers. The entity sells the vouchers through its website and the vouchers are non-refundable.

IE245 The entity and the restaurants jointly determine the prices at which the vouchers will be sold to customers. The entity is entitled to 30 per cent of the voucher price when it sells the voucher. The entity has no credit risk because the customers pay for the vouchers when purchased.

IE246 The entity also assists the customers in resolving complaints about the meals and has a buyer satisfaction programme. However, the restaurant is responsible for fulfilling obligations associated with the voucher, including remedies to a customer for dissatisfaction with the service.

IE247 To determine whether the entity is a principal or an agent, the entity ~~considers the nature of its promise and whether it takes control of the voucher (ie a right) before control transfers to the customer~~ identifies the specified good or service to be provided to the customer and assesses whether it controls the specified good or service before that good or service is transferred to the customer. ~~In making this determination, the entity considers the indicators in paragraph B37 of IFRS 15 as follows:~~

~~(a)~~ ~~the entity is not responsible for providing the meals itself, which will be provided by the restaurants;~~

~~(b)~~ ~~the entity does not have inventory risk for the vouchers because they are not purchased before being sold to customers and the vouchers are non-refundable;~~

~~(c)~~ ~~the entity has some discretion in setting the sales prices for vouchers to customers, but the sales prices are jointly determined with the restaurants; and~~

~~(d)~~ ~~the entity's consideration is in the form of a commission, because it is entitled to a stipulated percentage (30 per cent) of the voucher price.~~

IE247A The entity observes that the specified good or service to be provided to the customer is the right to a meal (in the form of a voucher) at a specified restaurant or restaurants, which the customer can use itself or transfer to another person. The entity also observes that no other promises are made to the customer.

IE247B The entity concludes that it does not control the right to the meal before that right is transferred to the customer. In reaching this conclusion, the entity principally considers the following:

(a) the vouchers are created only at the time that they are transferred to the customers and, thus, do not exist before that transfer. Therefore, the entity does not at any time have the ability to direct the use of the vouchers, or obtain substantially all of the remaining benefits from the vouchers, before they are transferred to customers.

(b) the entity neither purchases, nor commits to purchase, vouchers before they are sold to customers. The entity also has no responsibility to accept any returned vouchers. Therefore, the entity does not have inventory risk with respect to the vouchers as described in indicator (b) in paragraph B37 of IFRS 15.

(c) the entity does not provide a customer with the right to a meal and, then, contract with a restaurant to fulfil the entity's promise to provide that meal. Customers obtain vouchers for specific meals from restaurants that they select. In other words, the entity is not engaging the restaurants to provide a service of serving meals to customers on the entity's behalf as described in indicator (a) in paragraph B37 of IFRS 15.

IE248 ~~The entity concludes that its promise is to arrange for goods or services to be provided to customers (the purchasers of the vouchers) in exchange for a commission. On the basis of the indicators in paragraph B37 of IFRS 15, the entity concludes that it does not control the vouchers that provide a right to meals before they are transferred to the customers.~~ Thus, the entity concludes that it is an agent in the arrangement ~~and~~. The entity recognises revenue in the net amount of consideration to which the entity will be entitled in exchange for ~~the service~~ arranging for the restaurants to provide vouchers to customers for the restaurants' meals, which is the 30 per cent commission it is entitled to upon the sale of each voucher.

Example 48A—Entity is a principal and an agent in the same contract

IE248A An entity sells services to assist its customers in more effectively targeting potential recruits for open job positions. As part of the contract with a customer, the customer agrees to obtain a licence to access a third party's database of information on potential recruits. The entity arranges for this licence with the third party, but the customer contracts directly with the database provider for the licence. The entity collects payment on behalf of the third-party database provider as part of its overall invoicing to the customer. The database provider sets the price to the customer for the licence, and is responsible for providing technical support with the online application and providing credits to which the customer may be entitled for service down-time or other technical issues.

IE248B To determine whether the entity is a principal or an agent, the entity identifies the specified goods or services to be provided to the customer and assesses whether it controls those goods or services before they are transferred to the customer.

IE248C For the purpose of this example, it is assumed that the entity concludes that its recruitment services and the database access are two distinct goods or services based on its assessment of the requirements in paragraphs 27–30 of IFRS 15. Accordingly, the specified goods or services to be provided to the customer are access to the third party's database and recruitment services.

IE248D The entity concludes that it does not control the access to the database before it is provided to the customer. The entity does not at any time have the ability to direct the use of the licence because the customer contracts for the licence directly with the database provider. The entity does not control access to the provider's database—it cannot, for example, grant access to the database to a party other than the customer, or prevent the database provider from providing access to the customer.

IE248E As part of reaching that conclusion, the entity also considers the following indicators in paragraph B37 of IFRS 15. The entity concludes that these indicators provide further evidence that it does not control access to the database before that access is provided to the customer:

(a) the entity is not responsible for fulfilling the promise to provide the database access service. The customer contracts for the licence directly with the third-party database provider and the database provider is responsible for the acceptability of the database access (for example, by providing technical support or service credits).

(b) the entity does not have inventory risk because it does not purchase, or commit to purchase, the database access before the customer contracts for database access directly with the database provider, nor does it maintain the resources necessary to provide the database access.

(c) the entity does not have discretion in setting the price for the database access with the customer because the database provider sets that price.

IE248F Thus, the entity concludes that it is an agent in relation to the third party's database service. In contrast, the entity concludes that it is the principal in relation to the recruitment services because the entity performs those services itself and no other party is involved in providing them to the customer.

...

Example 54—Right to use intellectual property

IE276 Using the same facts as in Case A in Example 11 (see paragraphs IE49–IE53), the entity identifies four performance obligations in a contract:

(a) the software licence;

(b) installation services;

(c) software updates; and

(d) technical support.

IE277 The entity assesses the nature of its promise to transfer the software licence in accordance with paragraph B58 of IFRS 15. ~~The entity observes that the software is functional at the time that the licence transfers to the customer, and the customer can direct the use of, and obtain substantially all of the remaining benefits from, the software when the licence transfers to the customer. Furthermore, the entity concludes that because the software is functional when it transfers to the customer, the customer does not reasonably expect the entity to undertake activities that significantly affect the intellectual property to which the licence relates. This is because at the point in time that the licence is transferred to the customer, the intellectual property will not change throughout the licence period.~~ The entity does not consider in its assessment of the criteria in paragraph B58 of IFRS 15 the promise to provide software updates, because they ~~represent a separate performance obligation.~~ result in the transfer of an additional good or service to the customer (see paragraph B58(c)). The entity also observes that it does not have any contractual or implied obligations (independent of the updates and technical support) to undertake activities that will change the functionality of the software during the licence period. The entity observes that the software has significant stand-alone functionality and, therefore, the ability of the customer to obtain the benefits of the software is not substantially derived from the entity's ongoing activities. The entity therefore determines that the contract does not require, and the customer does not reasonably expect, the entity to undertake activities that significantly affect the software (independent of the updates and technical support). ~~Therefore, the~~ The entity concludes that none of the criteria in paragraph B58 of IFRS 15 are met and that the nature of the entity's promise in transferring the licence is to provide a right to use the entity's intellectual property as it exists at a point in time~~—ie the intellectual property to which the customer has rights is static~~. Consequently, the entity accounts for the licence as a performance obligation satisfied at a point in time.

Example 55—Licence of intellectual property

IE278 An entity enters into a contract with a customer to licence (for a period of three years) intellectual property related to the design and production processes for a good. The contract also specifies that the customer will obtain any updates to that intellectual property for new designs or production processes that may be developed by the entity. The updates are essential to the customer's ability to use the licence, because the customer operates in an industry in which technologies change rapidly. The entity does not sell the updates separately and the customer does not have the option to purchase the licence without the updates.

IE279 The entity assesses the goods and services promised to the customer to determine which goods and services are distinct in accordance with paragraph 27 of IFRS 15. The entity determines that although ~~the entity can conclude that~~ the customer can ~~obtain~~ benefit from the licence on its own without the updates ~~(see paragraph 27(a) of IFRS 15)~~, that benefit would be limited because the updates are critical to the customer's ability to continue to make use of the licence in the rapidly changing technological environment in which the customer operates. ~~In assessing whether the criterion in paragraph 27(b) of IFRS 15 is met, the~~ The entity observes that ~~the customer does not have the option to purchase the licence without the updates and the customer obtains limited benefit from the licence without the updates~~ its promise to the customer is to provide throughout the contract its most up-to-date intellectual property relating to the design and production process. The licence and the updates are, in effect, a subscription to the entity's intellectual property for a period of time. A customer generally would not separately acquire the initial licence because the updates are integral to its ability to use the entity's constantly evolving technology. This indicates that the licence is significantly affected by the promise to provide updates. Therefore, the entity concludes that its promise to grant the licence and its promise to provide the updates are highly dependent on, and interrelated ~~and the promise to grant the licence is not distinct within the context of the contract, because the licence is not separately identifiable from the promise to provide the updates (in accordance with the criterion in paragraph 27(b) and the factors in paragraph 29 of IFRS 15)~~ with, each other such that they constitute a single performance obligation to the customer.

IE280 The entity applies paragraphs 31–38 of IFRS 15 to determine whether the performance obligation (which includes the licence and the updates) is satisfied at a point in time or over time. The entity concludes that because the customer simultaneously receives and consumes the benefits of the entity's performance as it occurs, the performance obligation is satisfied over time in accordance with paragraph 35(a) of IFRS 15.

Example 56—Identifying a distinct licence

IE281 An entity, a pharmaceutical company, licenses to a customer its patent rights to an approved drug compound for 10 years and also promises to manufacture the drug for the customer. The drug is a mature product; therefore the entity will not undertake any activities to support the drug, which is consistent with its customary business practices.

Case A—Licence is not distinct

IE282 In this case, no other entity can manufacture this drug because of the highly specialised nature of the manufacturing process. As a result, the licence cannot be purchased separately from the manufacturing services.

IE283 The entity assesses the goods and services promised to the customer to determine which goods and services are distinct in accordance with paragraph 27 of IFRS 15. The entity determines that the customer cannot benefit from the licence without the manufacturing service; therefore, the criterion in paragraph 27(a) of IFRS 15 is not met. Consequently, the licence and the manufacturing service are not distinct and the entity accounts for the licence and the manufacturing service as a single performance obligation.

IE284 The entity applies paragraphs 31–38 of IFRS 15 to determine whether the performance obligation (ie the bundle of the licence and the manufacturing services) is a performance obligation satisfied at a point in time or over time.

Case B—Licence is distinct

IE285 In this case, the manufacturing process used to produce the drug is not unique or specialised and several other entities can also manufacture the drug for the customer.

IE286 The entity assesses the goods and services promised to the customer to determine which goods and services are distinct in accordance with paragraph 27 of IFRS 15. Because the manufacturing process can be provided by other entities, the entity concludes that the customer can benefit from the licence ~~on its own (ie without the manufacturing service)~~ together with readily available resources (ie manufacturing service provided by a third party) and also concludes that the customer can benefit from the manufacturing service together with the licence transferred to the customer at the start of the contract. Thus, the criterion in paragraph 27(a) of IFRS 15 is met. The entity also determines that the licence is separately identifiable from the manufacturing process (ie the ~~criteria~~ criterion in paragraph 27(b) of IFRS 15 ~~are~~ is met). Neither the licence, nor the manufacturing service, is significantly modified or customised by the other and the entity has not promised to provide a significant integration service that transforms the licence and the manufacturing service into a combined output. Even though the manufacturing service depends on the licence, the entity can fulfil its promise to transfer the licence, and the customer could benefit from the licence, independently of this service.

Similarly, the customer could acquire the licence separately without significantly affecting the entity's promise to manufacture the drug. Consequently, the entity concludes that the licence and the manufacturing service are distinct and the entity has two performance obligations:

(a) licence of patent rights; and

(b) manufacturing service.

IE287 The entity assesses, in accordance with paragraph B58 of IFRS 15, the nature of the entity's promise to grant the licence. The drug is a mature product (ie it has been approved, is currently being manufactured and has been sold commercially for the last several years). For these types of mature products, the entity's customary business practices are not to undertake any activities to support the drug. The drug formula has significant stand-alone functionality (ie its ability to produce a drug that treats a disease or condition) and, therefore, the ability of the customer to obtain the benefits of the drug formula is not substantially derived from the entity's ongoing activities. Consequently, the entity concludes that the criteria in paragraph B58 of IFRS 15 are not met because the contract does not require, and the customer does not reasonably expect, the entity to undertake activities that significantly affect the intellectual property to which the customer has rights. In its assessment of the criteria in paragraph B58 of IFRS 15, the entity does not take into consideration the separate performance obligation of promising to provide a manufacturing service. Consequently, the nature of the entity's promise in transferring the licence is to provide a right to use the entity's intellectual property in the form and the functionality with which it exists at the point in time that it is granted to the customer. Consequently, the entity accounts for the licence as a performance obligation satisfied at a point in time.

IE288 The entity applies paragraphs 31–38 of IFRS 15 to determine whether the manufacturing service is a performance obligation satisfied at a point in time or over time.

Example 57—Franchise rights

IE289 An entity enters into a contract with a customer and promises to grant a franchise licence that provides the customer with the right to use the entity's trade name and sell the entity's products for 10 years. In addition to the licence, the entity also promises to provide the equipment necessary to operate a franchise store. In exchange for granting the licence, the entity receives a sales-based royalty of five per cent of the customer's monthly sales. The fixed consideration for the equipment is CU150,000 payable when the equipment is delivered.

Identifying performance obligations

IE290 The entity assesses the goods and services promised to the customer to determine which goods and services are distinct in accordance with paragraph 27 of IFRS 15. The entity observes that the entity, as a franchisor, has developed a customary business practice to undertake activities such as analysing the customer's changing preferences and implementing product improvements, pricing strategies, marketing campaigns and operational efficiencies to support the franchise name. However, the entity concludes that these activities do not directly transfer goods or services to the customer because they are part of the entity's promise to grant a licence ~~and, in effect, change the intellectual property to which the customer has rights~~.

IE291 The entity determines that it has two promises to transfer goods or services: a promise to grant a licence and a promise to transfer equipment. In addition, the entity concludes that the promise to grant the licence and the promise to transfer the equipment are distinct. This is because the customer can benefit from each promise (ie the promise of the licence and the promise of the equipment) on their own or together with other resources that are readily available (see paragraph 27(a) of IFRS 15). (That is, the customer can benefit from the licence together with the equipment that is delivered before the opening of the franchise and the equipment can be used in the franchise or sold for an amount other than scrap value.) The entity also determines that the franchise licence and equipment are separately identifiable, in accordance with the criterion in paragraph 27(b) of IFRS 15~~, because none of the factors in paragraph 29 of IFRS 15 are present~~. The entity has not promised to provide a significant integration service that transforms the licence and the equipment into a combined output and neither the licence, nor the equipment, is significantly modified or customised by the other. In addition, the entity could fulfil either promise independently of the other. If the customer decided not to purchase the equipment, it would not affect the entity's promise to grant the licence to the customer. Similarly, if the customer acquired the licence separately, it would not affect the entity's promise to transfer the equipment. Consequently, the entity has two performance obligations:

(a) the franchise licence; and

(b) the equipment.

Allocating the transaction price

IE292 The entity determines that the transaction price includes fixed consideration of CU150,000 and variable consideration (five per cent of customer sales).

IE293 The entity applies paragraph 85 of IFRS 15 to determine whether the variable consideration should be allocated entirely to the performance obligation to transfer the franchise licence. The entity concludes that the variable consideration (ie the sales-based royalty) should be allocated entirely to the franchise licence because the variable consideration relates entirely to the entity's promise to grant the franchise licence. In addition, the entity observes that allocating CU150,000 to the equipment and the sales-based royalty to the franchise licence would be consistent with an allocation based on the entity's relative stand-alone selling prices in similar contracts. That is, the stand-alone selling price of the equipment is CU150,000 and the entity regularly licences franchises in exchange for five per cent of customer sales. Consequently, the entity concludes that the variable consideration (ie the sales-based royalty) should be allocated entirely to the performance obligation to grant the franchise licence.

Application guidance: licensing

IE294 The entity assesses, in accordance with paragraph B58 of IFRS 15, the nature of the entity's promise to grant the franchise licence. The entity concludes that the criteria in paragraph B58 of IFRS 15 are met and the nature of the entity's promise is to provide access to the entity's intellectual property in its current form throughout the licence period. This is because:

(a) the entity concludes that the customer would reasonably expect that the entity will undertake activities that will significantly affect the intellectual property to which the customer has rights. The ability of the customer to obtain benefit from the intellectual property to which the customer has rights is substantially derived from, or dependent upon, the expected activities of the entity. This is on the basis of the entity's customary business practice to undertake activities such as analysing the customer's changing preferences and implementing product improvements, pricing strategies, marketing campaigns and operational efficiencies. In addition, the entity observes that because part of its compensation is dependent on the success of the franchisee (as evidenced through the sales-based royalty), the entity has a shared economic interest with the customer that indicates that the customer will expect the entity to undertake those activities to maximise earnings.

(b) the entity also observes that the franchise licence requires the customer to implement any changes that result from those activities and thus exposes the customer to any positive or negative effects of those activities.

(c) the entity also observes that even though the customer may benefit from the activities through the rights granted by the licence, they do not transfer a good or service to the customer as those activities occur.

IE295 Because the criteria in paragraph B58 of IFRS 15 are met, the entity concludes that the promise to transfer the licence is a performance obligation satisfied over time in accordance with paragraph 35(a) of IFRS 15.

IE296 The entity also concludes that because the consideration is in the form of a sales-based royalty that relates specifically to the franchise licence (see paragraph B63B), the entity applies paragraph B63 of IFRS 15 and, after the transfer of the franchise licence, the entity recognises revenue as and when those sales occur.

Example 58—Access to intellectual property

IE297 An entity, a creator of comic strips, licenses the use of the images and names of its comic strip characters in three of its comic strips to a customer for a four-year term. There are main characters involved in each of the comic strips. However, newly created characters appear regularly and the images of the characters evolve over time. The customer, an operator of cruise ships, can use the entity's characters in various ways, such as in shows or parades, within reasonable guidelines. The contract requires the customer to use the latest images of the characters.

IE298 In exchange for granting the licence, the entity receives a fixed payment of CU1 million in each year of the four-year term.

IE299 In accordance with paragraph 27 of IFRS 15, the entity assesses the goods and services promised to the customer to determine which goods and services are distinct. The entity concludes that it has no other performance obligations other than the promise to grant a licence. That is, the additional activities associated with the licence do not directly transfer a good or service to the customer because they are part of the entity's promise to grant a licence ~~and, in effect, change the intellectual property to which the customer has rights~~.

IE300 The entity assesses the nature of the entity's promise to transfer the licence in accordance with paragraph B58 of IFRS 15. In assessing the criteria the entity considers the following:

(a) the customer reasonably expects (arising from the entity's customary business practices) that the entity will undertake activities that will significantly affect the intellectual property to which the customer has rights (ie the characters). ~~Those activities include development of the characters and the publishing of a weekly comic strip that includes the characters~~ This is because the entity's activities (ie development of the characters) change the form of the intellectual property to which the customer has rights. Further, the ability of the customer to obtain benefit from the intellectual property to which the customer has rights is substantially derived from, or dependent upon, the entity's activities (ie the publishing of the comic strip).

(b) the rights granted by the licence directly expose the customer to any positive or negative effects of the entity's activities because the contract requires the customer to use the latest characters.

(c) even though the customer may benefit from those activities through the rights granted by the licence, they do not transfer a good or service to the customer as those activities occur.

IE301 Consequently, the entity concludes that the criteria in paragraph B58 of IFRS 15 are met and that the nature of the entity's promise to transfer the licence is to provide the customer with access to the entity's intellectual property as it exists throughout the licence period. Consequently, the entity accounts for the promised licence as a performance obligation satisfied over time (ie the criterion in paragraph 35(a) of IFRS 15 is met).

IE302 The entity applies paragraphs 39–45 of IFRS 15 to identify the method that best depicts its performance in the licence. Because the contract provides the customer with unlimited use of the licensed characters for a fixed term, the entity determines that a time-based method would be the most appropriate measure of progress towards complete satisfaction of the performance obligation.

Example 59—Right to use intellectual property

IE303 An entity, a music record label, licenses to a customer a 1975 recording of a classical symphony by a noted orchestra. The customer, a consumer products company, has the right to use the recorded symphony in all commercials, including television, radio and online advertisements for two years in Country A. In exchange for providing the licence, the entity receives fixed consideration of CU10,000 per month. The contract does not include any other goods or services to be provided by the entity. The contract is non-cancellable.

IE304 The entity assesses the goods and services promised to the customer to determine which goods and services are distinct in accordance with paragraph 27 of IFRS 15. The entity concludes that its only performance obligation is to grant the licence.

IE305 In accordance with paragraph B58 of IFRS 15, the entity assesses the nature of the entity's promise to grant the licence. The entity does not have any contractual or implied obligations to change the licensed recording. ~~Thus, the intellectual property to which the customer has rights is static.~~ The licensed recording has significant stand-alone functionality (ie the ability to be played) and, therefore, the ability of the customer to obtain the benefits of the recording is not substantially derived from the entity's ongoing activities. The entity therefore determines that the contract does not require, and the customer does not reasonably expect, the entity to undertake activities that significantly affect the licensed recording. Consequently, the entity concludes that the nature of its promise in transferring the licence is to provide the customer with a right to use the entity's intellectual property as it exists at the point in time that it is granted. Therefore, the promise to grant the licence is a performance obligation satisfied at a point in time. The entity recognises all of the revenue at the point in time when the customer can direct the use of, and obtain substantially all of the remaining benefits from, the licensed intellectual property.

IE306 Because of the length of time between the entity's performance (at the beginning of the period) and the customer's monthly payments over two years (which are non-cancellable), the entity considers the requirements in paragraphs 60–65 of IFRS 15 to determine whether a significant financing component exists.

Example 60—Sales-based royalty for a licence of intellectual property

IE307 An entity, a movie distribution company, licenses Movie XYZ to a customer. The customer, an operator of cinemas, has the right to show the movie in its cinemas for six weeks. Additionally, the entity has agreed to (a) provide memorabilia from the filming to the customer for display at the customer's cinemas before the beginning of the six week screening period; and (b) sponsor radio advertisements for Movie XYZ on radio stations in the customer's geographic area throughout the six week screening period. In exchange for providing the licence and the additional promotional goods and services, the entity will receive a portion of the operator's ticket sales for Movie XYZ (ie variable consideration in the form of a sales-based royalty). ~~The entity concludes that its only performance obligation is the promise to grant the licence.~~

IE308 ~~The entity observes that regardless of whether the promise to grant the licence represents a right to access the entity's intellectual property, or a right to use the entity's intellectual property, the entity applies paragraph B63 of IFRS 15 and recognises revenue as and when the ticket sales occur. This is because the consideration for its licence of intellectual property is a sales-based royalty and~~

~~the entity has already transferred the licence to the movie to which the sales-based royalty relates.~~ In this example, the entity is not required to evaluate whether the licence and the other promotional goods and services are distinct. This is because, regardless of whether each of those promised goods or services are performance obligations, the entity concludes that the licence to show Movie XYZ is the predominant item to which the sales-based royalty relates. Therefore, the entity will recognise revenue from the sales-based royalty, the only consideration to which the entity is entitled under the contract, in accordance with paragraph B63.

Example 61—Access to intellectual property

IE309 An entity, a well-known sports team, licenses the use of its name and logo to a customer. The customer, an apparel designer, has the right to use the sports team's name and logo on items including t-shirts, caps, mugs and towels for one year. In exchange for providing the licence, the entity will receive fixed consideration of CU2 million and a royalty of five per cent of the sales price of any items using the team name or logo. The customer expects that the entity will continue to play games and provide a competitive team.

IE310 The entity assesses the goods and services promised to the customer to determine which goods and services are distinct in accordance with paragraph 27 of IFRS 15. The entity concludes that its only performance obligation is to transfer the licence. ~~That is, the~~ The additional activities associated with the licence (ie continuing to play games and provide a competitive team) do not directly transfer a good or service to the customer because they are part of the entity's promise to grant the licence ~~and, in effect, change the intellectual property to which the customer has rights~~.

IE311 The entity assesses the nature of the entity's promise to transfer the licence in accordance with paragraph B58 of IFRS 15. In assessing the criteria the entity considers the following:

(a) the entity concludes that the customer would reasonably expect that the entity will undertake activities that will significantly affect the intellectual property (ie the team name and logo) to which the customer has rights. The ability of the customer to obtain benefit from the name and logo is substantially derived from, or dependent upon, the expected activities of the entity. This is on the basis of the entity's customary business practice to undertake activities such as continuing to play and providing a competitive team. In addition, the entity observes that because some of its consideration is dependent on the success of the customer (through the sales-based royalty), the entity has a shared economic interest with the customer, which indicates that the customer will expect the entity to undertake those activities to maximise earnings.

(b) the entity observes that the rights granted by the licence (ie the use of the team's name and logo) directly expose the customer to any positive or negative effects of the entity's activities.

(c) the entity also observes that even though the customer may benefit from the activities through the rights granted by the licence, they do not transfer a good or service to the customer as those activities occur.

IE312 The entity concludes that the criteria in paragraph B58 of IFRS 15 are met and the nature of the entity's promise to grant the licence is to provide the customer with access to the entity's intellectual property as it exists throughout the licence period. Consequently, the entity accounts for the promised licence as a performance obligation satisfied over time (ie the criterion in paragraph 35(a) of IFRS 15 is met).

IE313 The entity then applies paragraphs 39–45 of IFRS 15 to determine a measure of progress that will depict the entity's performance for the fixed consideration. For the consideration that is in the form of a sales-based royalty, paragraph B63 of IFRS 15 applies <u>because the sales-based royalty relates solely to the licence that is the only performance obligation in the contract</u>; therefore, the entity recognises revenue as and when the sales of items using the team name or logo occur.

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The Exposure Draft *Clarifications to IFRS 15* was approved for publication by thirteen members of the International Accounting Standards Board. Mr Ochi voted against its publication. His alternative view is set out after the Basis for Conclusions.

Hans Hoogervorst	Chairman
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Basis for Conclusions on the Exposure Draft *Clarifications to IFRS 15*

This Basis for Conclusions accompanies, but is not part of, the proposed amendments.

Background

BC1 This Basis for Conclusions summarises the considerations of the International Accounting Standards Board (IASB) when developing the amendments proposed in the Exposure Draft *Clarifications to IFRS 15*. Individual IASB members gave greater weight to some factors than to others.

BC2 Since the issuance of IFRS 15 *Revenue from Contracts with Customers* and Financial Accounting Standards Board (FASB) Topic 606 *Revenue from Contracts with Customers* in May 2014[1], some issues arising from the discussions of the Transition Resource Group for Revenue Recognition (TRG) have been discussed jointly by the IASB and the FASB (collectively, the 'Boards'). Based on those discussions, the IASB and the FASB have each decided whether to undertake standard setting to address these issues.

BC3 In reaching its decisions, the IASB observed that amendments to a recently issued standard create a risk of unintended consequences and may place an unwarranted burden on some stakeholders, such as the need in some jurisdictions to translate the amendments and incorporate them into a Standard that may be partly through its endorsement process. Amendments could also be disruptive to the implementation process that is already underway and potentially generate undue costs if entities have to revisit the implementation work that they have already performed. The IASB also observed that it is expected that questions relating to new requirements will arise during the initial period after a new Standard is issued, which are generally resolved as stakeholders gain a better understanding of the new requirements. In addition, the TRG's and the Boards' discussions about potential implementation issues serve as useful education materials to stakeholders.

BC4 Consequently, the IASB decided to apply a high hurdle when considering whether to amend the Standard and, thus, to minimise changes to the extent possible. On this basis, the IASB is proposing amendments to the Standard only when (a) it considers those proposed amendments to be essential to clarifying the Boards' intentions when developing the requirements in IFRS 15; or (b) it views the benefits of retaining converged requirements as greater than any potential costs of amending the requirements (for example, in respect of the principal versus agent considerations). The IASB is also proposing more extensive changes to some of the Illustrative Examples accompanying IFRS 15. The IASB concluded that clarifications can often be made more effectively in the examples, rather than by amending the Standard.

BC5 Both the IASB and FASB decided to propose amendments with respect to identifying performance obligations, principal versus agent considerations and

1 Unless indicated otherwise, references to IFRS 15 in this Basis for Conclusions can be read as also referring to Topic 606.

licensing, as well as proposing new transition relief for modified contracts. Apart from the clarifications regarding principal versus agent considerations, the extent of the proposed amendments and the wording of the Boards' proposed amendments is not (or is not expected to be) the same. The IASB is also proposing transition relief with respect to completed contracts and the FASB is expected to propose amendments with respect to collectability, measuring non-cash consideration and a practical expedient relating to the presentation of sales taxes. An overview of the considerations of each Board in reaching its decisions is explained in this Basis for Conclusions. Because of the different decisions made, the IASB and the FASB have each published (or are to publish) their proposals in separate Exposure Drafts, which have differing comment periods.

BC6 The following table summarises the respective decisions of the Boards.

Issues for which both the IASB and the FASB have decided to undertake standard setting

Issue	IASB proposals	FASB proposals	Reference
Determining when a good or service is 'separately identifiable'	Amendments to the Illustrative Examples accompanying IFRS 15 (using similar fact patterns to the FASB proposals)	Amendments to the Codification (including Illustrations)	paragraphs BC8–BC16
Determining whether an entity is a principal or an agent	Amendments to IFRS 15 and accompanying Illustrative Examples	Amendments to the Codification (including Illustrations)	paragraphs BC26–BC56
Determining the nature of an entity's promise in granting a licence	Amendments to IFRS 15 and accompanying Illustrative Examples	Amendments to the Codification (including Illustrations)	paragraphs BC59–BC70
Application of the exemption for sales- and usage-based royalties	Amendments to IFRS 15 and accompanying Illustrative Examples	Amendments to the Codification (including Illustrations)	paragraphs BC71–BC79
Practical expedients upon transition	Amendments to IFRS 15	Amendments to the Codification	paragraphs BC109–BC115

Issues for which the IASB decided not to undertake standard-setting but the FASB has proposed (or is expected to propose) amendments to Topic 606

Issue	FASB proposals	Reference
Identification of promised goods or services (materiality considerations)	Amendments to the Codification (including Illustrations)	paragraphs BC17–BC21

continued...

...continued

Issue	FASB proposals	Reference
Shipping and handling activities	Amendments to the Codification	paragraphs BC22–BC24
How contractual restrictions in a licence affect the identification of promises	Amendments to the Codification (including Illustrations)	paragraphs BC80–BC82
Determining when an entity should assess the nature of a licence	Amendments to the Codification	paragraphs BC83–BC86
Collectability (assessing collectability / contract termination)	Amendments to the Codification (including Illustrations)	paragraphs BC87–BC97
Non-cash consideration (measurement date / variability)	Amendments to the Codification (including Illustrations)	paragraphs BC98–BC104
Presentation of sales taxes	Amendments to the Codification	paragraphs BC105–BC108

Identifying performance obligations

BC7 IFRS 15 requires an entity to identify performance obligations on the basis of whether the promised goods or services are distinct using a two-step process:

(a) The first step is to determine whether the good or service is capable of being distinct in accordance with paragraph 27(a). This criterion specifies a minimum characteristic or attribute of a good or service underlying a performance obligation (ie a 'floor') to prevent overly granular disaggregation of the contract. The customer must be able to benefit from the good or service underlying a performance obligation either on its own or together with other resources that are readily available to the customer. This criterion is supported by guidance in paragraph 28.

(b) The second step is to determine whether the promise to transfer a good or service is separately identifiable from other promises in the contract in accordance with paragraph 27(b). This criterion assesses whether a good or service that is capable of being distinct (in accordance with paragraph 27(a)) retains its distinct character within the context of the other goods or services promised in the contract.

Distinct goods or services

BC8 The TRG considered issues relating to the criterion in paragraph 27(b) regarding when a promised good or service is separately identifiable (ie distinct within the context of a contract) and the supporting factors in paragraph 29. The discussion informed the Boards about potential diversity in stakeholders' understanding of the principle in paragraph 27(b) and supporting factors in paragraph 29. In particular, the TRG's discussion indicated that there is a risk of paragraph 29(c) being applied more broadly than intended, resulting in items being inappropriately combined as a single performance obligation. Stakeholders asked about the application of this factor to scenarios in which one of the promised goods or services is dependent on the transfer of the other, such as a contract for equipment and related consumables that are required for the equipment to function. Some stakeholders suggested that, although the promised goods or services may be capable of being distinct, if one of the goods or services was dependent on the other, the promised goods or services would not be distinct within the context of the contract.

BC9 In the light of those discussions and the feedback received, the IASB is proposing to add some new examples, and to amend some of the existing examples that accompany IFRS 15, to clarify how an entity should apply the requirements on identifying performance obligations. The IASB is of the view that the TRG's discussions highlighted educational needs and that, given the nature of the issues raised, amendments to the Standard are not required. In reaching its decision, the IASB observed that the concept of 'distinct within the context of the contract' is new and, thus, it is expected that questions will arise as practice develops. Applying the principle in paragraph 27(b) requires judgement, taking into account facts and circumstances. Amendments to the requirements in IFRS 15 would not affect the need to apply judgement in determining whether promised goods or services are distinct.

BC10 The TRG's discussions indicated that there was some confusion relating to the criteria in paragraph 27 and the role of the supporting factors in paragraph 29. The IASB observed that the criterion in paragraph 27(b) focuses on the separability of the promise to transfer a good or service, rather than on the good or service itself. This emphasises that an entity should evaluate whether the contract is to transfer (a) multiple distinct goods or services or (b) a combined item or items that comprise a distinct bundle of goods or services promised in the contract. The factors in paragraph 29 highlight situations in which a good or service that is capable of being distinct is not distinct within the context of the contract because the goods or services are combined or modified. In other words, those factors highlight scenarios in which the entity may have promised to transfer something that is greater than (or substantively different from) the sum of the underlying promised goods and services. For example, in a contract to build a wall, the promise to provide bricks and the promise to provide labour are not separately identifiable from each other within the context of the contract because those promises together comprise the promise to the customer to build the wall.

BC11 The evaluation of whether an entity's promise to transfer a good or service is separately identifiable from other promises in the contract considers the relationship between the various goods or services within the contract in the context of the process of fulfilling the contract. That is, an entity should consider the level of integration, interrelation or interdependence among promises to transfer goods or services. The IASB observed that an entity should not merely evaluate whether one item, by its nature, depends on the other (ie whether two items have a functional relationship). Instead, an entity should evaluate whether there is a transformative relationship between the two items in the process of fulfilling the contract. In many cases, it may be helpful for an entity to consider whether it could fulfil its promises to transfer goods or services to the customer independently of each other.

BC12 The TRG's discussions also highlighted that some stakeholders may be applying the factors supporting paragraph 27(b) as a series of criteria. Paragraph 29 provides a non-exhaustive list of factors that indicate that an entity's promise to transfer a good or service is separately identifiable. As discussed in paragraph BC104 of IFRS 15, the Boards decided not to express these factors as criteria because doing so could be too restrictive and might force bundling or unbundling that does not reflect the economics of the arrangement. The Boards did not intend paragraph 29 to be read as a series of criteria—ie not all of the factors need to be met to conclude that a promise is separately identifiable.

BC13 Stakeholders also asked about the effect of contractual restrictions on the identification of performance obligations. Accordingly, the IASB is proposing a new example (Case D of Example 11) that illustrates the Boards' observation in paragraph BC100 of IFRS 15 that an entity should focus on the characteristics of the goods or services themselves instead of the way in which the customer might use the goods or services.

BC14 The FASB has proposed amending Topic 606 to expand the articulation of the separately identifiable principle and to reframe the existing factors in paragraph 606-10-25-21 (paragraph 29 of IFRS 15) to align them with the amended principle. The FASB is of the view that its proposed amendments would better describe the Boards' intentions and would not be a change in the underlying principle. The FASB's proposed amendments include the following:

(a) explaining that the objective when assessing whether an entity's promises to transfer goods or services to the customer are separately identifiable is to determine whether the nature of the entity's overall promise in the contract is to transfer each of those goods or services or whether the promise is to transfer a combined item or items to which the goods or services are inputs.

(b) putting into the plural particular words to clarify that (i) the factors should be evaluated to assess whether the promised goods or services significantly affect each other (rather than whether one promised good or service significantly affects the other); and (ii) a combined output may include more than one phase, element, or unit.

(c) reframing the factors to identify when the promises are not separately identifiable rather than when they are separately identifiable.

BC15 The FASB has also proposed additional examples to illustrate how to identify performance obligations. The new examples proposed by the IASB to accompany IFRS 15 have similar fact patterns to the FASB's proposals and reach consistent conclusions. However, the IASB decided not to include a new example proposed by the FASB relating to the evaluation of whether an anti-virus software licence is distinct from when-and-if-available updates to the software during the licence period (Example 10, Case C in the FASB proposals). The IASB does not think that an additional example is required because Example 55 that accompanies IFRS 15 already illustrates application of the requirements on identifying performance obligations to a similar fact pattern.

BC16 Lastly, the FASB proposals include revisions to the existing examples in Topic 606 to reflect the following:

(a) rearticulation of the separately identifiable principle;

(b) amendments to the factors in paragraph 606-10-25-21 (paragraph 29 of IFRS 15);

(c) drafting proposals intended to demonstrate more clearly how the FASB intends the separation guidance to be applied;

(d) replacing 'distinct within the context of the contract' with 'separately identifiable' in order to clarify that both terms encompass the same concept; and

(e) other proposed editorial changes.

Promised goods or services

BC17 The TRG discussed an implementation question about whether an entity should identify items or activities as promised goods or services that are not identified as deliverables or components under previous revenue Standards. A specific concern was raised about paragraph BC90 of IFRS 15, which explains the Boards' decision not to exempt an entity from accounting for performance obligations that the entity might regard as being 'perfunctory or inconsequential' (a notion that is included in guidance issued by the staff of the US Securities and Exchange Commission). Some stakeholders held a view that IFRS 15 might require an entity to identify significantly more performance obligations than would be the case under previous revenue Standards.

BC18 In response to these concerns, the FASB has proposed an amendment that would permit an entity not to identify promised goods or services that are immaterial in the context of the contract. This is because the FASB is concerned that it would be unduly burdensome to require an entity to aggregate and determine the effect on its financial statements of those items or activities determined to be immaterial at the contract level. However, its proposals emphasise that optional goods or services continue to be accounted for in accordance with paragraphs 606-10-55-41 through 55-45 (paragraphs B39–B43 of IFRS 15).

BC19 Having considered the wider implications of amending IFRS 15 at this time (described in paragraph BC3), the IASB decided not to propose incorporating similar guidance into IFRS 15. The TRG's discussion highlighted that the concerns raised primarily relate to potential changes to practice under US GAAP. Previous revenue Standards under IFRS do not contain similar language to the guidance issued by the staff of the US Securities and Exchange Commission on inconsequential or perfunctory performance obligations. The TRG's discussion indicated that IFRS stakeholders can understand and apply the requirements of IFRS 15. IFRS stakeholders have not expressed concerns about making reasonable judgements when assessing the promised goods or services in a contract for the purpose of identifying performance obligations.

BC20 The IASB is of the view that the concerns raised relate to the application of materiality concepts rather than the application of the requirements in IFRS 15. As described in paragraph BC84 of IFRS 15, the Boards intended the notion of a performance obligation to be similar to the notions of deliverables, components or elements of a contract in previous revenue Standards. The IASB noted that IFRS 15 requires an entity to identify performance obligations rather than promised goods or services. Accordingly, although an entity makes an assessment of the goods or services promised in a contract in order to identify material performance obligations, the IASB did not intend to require an entity to individually identify every possible promised good or service.

BC21 In reaching its decision, the IASB also observed that the explanation in paragraph BC90 of IFRS 15 should be read in the context of the Boards' explanation of the development of IFRS 15 rather than as implying that an entity is required to identify perfunctory or inconsequential goods or services promised in a contract. One of the reasons that the IASB decided not to introduce an exemption for perfunctory or inconsequential performance obligations is that it was not considered necessary, both because of how the concept of 'distinct' is applied and also because of the application of materiality. In assessing promised goods or services and identifying performance obligations, entities need to consider the overall objective of IFRS 15 as well as materiality considerations.

Shipping and handling activities

BC22 Some stakeholders in the US have expressed differing views about whether and when shipping and handling activities that occur after the transfer of control to the customer should be accounted for as a promised service or as a fulfilment activity. Under previous revenue Standards, entities often do not account for shipping provided in conjunction with the sale of their goods as an additional service. As a result, some stakeholders raised cost benefit concerns and questioned whether additional relief should be provided.

BC23 The FASB has proposed an amendment to Topic 606 to state explicitly the Boards' view that shipping and handling activities that occur before the customer obtains control of the related good are fulfilment activities. In addition, the FASB has proposed to permit an entity, as an accounting policy election, to account for shipping and handling activities that occur after the customer has obtained control of a good as fulfilment activities. In reaching its conclusions, the FASB explained that it decided to provide an accounting policy election because it expects the election to improve the operability of the new revenue Standard without diminishing the information provided to users of financial statements. The FASB noted that a change in practice for entities that do not account for shipping and handling activities as a deliverable under previous US revenue Standards could be costly to implement and apply on an ongoing basis.

BC24 Having considered the wider implications of amending IFRS 15 at this time (described in paragraph BC3), the IASB has not proposed a similar amendment on the basis that an accounting policy election for shipping and handling activities would create an exception to the revenue recognition model and potentially reduce comparability between entities. Paragraph 22 requires an entity to assess the goods or services promised in a contract with a customer in order to identify performance obligations. The introduction of a policy election would override this requirement. In addition, a policy election is applicable to all entities. Consequently, it is possible that entities with significant shipping operations could make different policy elections. This would make it more difficult for users of financial statements to understand and compare the revenue reported by different entities, including those within the same industry.

Other changes proposed by the FASB on this topic

BC25 Paragraph 24 states that an implied promise in a contract with a customer may exist if a promise creates a valid expectation of the customer that the entity will transfer a good or service to the customer. The FASB has proposed to change the term 'valid' to 'reasonable' as a result of questions raised by US stakeholders about the meaning of 'valid'. This is because paragraph BC87 of IFRS 15 states that implied promises do not need to be enforceable by law. The IASB observed that use of the term 'valid' is consistent with guidance relating to constructive obligations in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. Therefore, it concluded that making a similar amendment to paragraph 24 would create inconsistencies within IFRS and, consequently, decided not to propose an amendment.

Principal versus agent considerations

BC26 When another party, in addition to the entity, is involved in providing goods or services to a customer, IFRS 15 requires the entity to determine whether it is:

(a) the principal in the transaction (recognising as revenue the gross amount of consideration to which it expects to be entitled in exchange for providing the specified goods or services to the customer); or

(b) the agent (recognising as revenue the fee or commission for arranging for the other party to provide the specified goods or services to the customer).

Paragraphs B34–B38 include guidance to help an entity make that determination.

BC27 The TRG discussed a number of issues regarding the guidance in paragraphs B34–B38. Some stakeholders questioned whether control is always the basis for determining whether an entity is a principal or an agent, and how the control principle and the indicators in paragraph B37 work together. Other stakeholders questioned how to apply the control principle to contracts involving intangible goods or services.

BC28 In the light of those discussions, the Boards discussed whether and how to clarify the principal versus agent guidance in paragraphs B34–B38.

Principle for determining whether an entity is a principal or an agent

BC29 Paragraph B34 requires an entity to determine whether it is a principal or an agent based on whether the nature of the entity's promise is a performance obligation to *provide* the specified goods or services itself (ie the entity is a principal) or to *arrange* for those goods or services to be provided by another party (ie the entity is an agent). Assessing whether the entity controls the specified good or service is the basis for determining the nature of the entity's promise.

BC30 The Boards observed that in order for an entity to conclude that it is providing the specified good or service to the customer, it must first control that good or service (as defined in paragraph 33). It would be difficult for an entity to provide the specified good or service to a customer if the entity does not first have (and control) that good or service to be provided. If an entity controls the specified good or service before that good or service is transferred to the customer, it is the principal in the transaction with the customer. If the entity does not control the specified good or service before it is transferred to a customer, it is not a principal in the transaction with the customer. The Boards noted that their considerations in this respect are explained in paragraph BC380 of IFRS 15.

BC31 In addition, the Boards noted that an entity that itself manufactures a good or performs a service is always a principal if the entity transfers control of that good or service to another party. Such an entity does not evaluate whether it is a principal or an agent using the guidance in paragraphs B34–B38 because the entity transfers the good or provides the service directly to its customer, without the involvement of another party. If the entity transfers a good or provides a service to an intermediary that is a principal in providing that good or service to an end customer (whether individually or as part of a distinct bundle of goods or services), the entity's customer is the intermediary.

BC32 Because of the concerns highlighted in the TRG's discussions, the Boards decided to clarify the following aspects of the guidance on principal versus agent considerations:

(a) The relationship between the control principle and the indicators in paragraph B37.

(b) Applying control to intangible goods or services.

BC33 Throughout the guidance on principal versus agent considerations, the Boards decided to refer to the 'specified good or service' transferred to the customer (as in paragraph B34), rather than the 'performance obligation'. This is because use of the term 'performance obligation' would have been confusing if an entity is an agent. An agent's performance obligation is to arrange for goods or services to be provided by another party; it does not promise to provide the goods or services itself to the end customer. Accordingly, the specified good or service to be provided to the end customer is not the performance obligation of the agent.

The relationship between control and the indicators in paragraph B37

BC34 The Boards observed that the questions regarding the relationship between the assessment of control and the indicators of control in paragraph B37, at least in part, arise because the indicators in paragraph B37 are carried forward from IAS 18 *Revenue* and Topic 605, *Revenue Recognition*. IAS 18 had a principle for this assessment (based on risks and rewards) that was different from the control principle in IFRS 15 and, although Topic 605 did not explicitly include a principle, the indicators in Topic 605 were understood to be indicators of risks and rewards. In addition, the structure of the analysis in Examples 45–48 accompanying IFRS 15 has added to the confusion.

BC35 The Boards' considerations (explained in paragraph BC382 of IFRS 15) highlight that the indicators in paragraph B37 were included to support an entity's assessment of whether it controls a specified good or service before transfer in scenarios for which that assessment might be difficult. The indicators (a) do not override the assessment of control; (b) should not be viewed in isolation; (c) do not constitute a separate or additional evaluation; and (d) should not be considered a checklist of criteria to be met, or factors to be considered, in all scenarios. Considering one or more of the indicators will often be helpful and, depending on the facts and circumstances, individual indicators will be more or less relevant or persuasive to the assessment of control.

BC36 The Boards acknowledged that the indicators are similar to those in IAS 18 and Topic 605, but also noted their considerations in this respect explained in paragraph BC382 of IFRS 15. Paragraph BC382 explains that the Boards decided to carry over some of the indicators in previous revenue recognition Standards even though those indicators have a different purpose in the new Standard. In the new Standard, the indicators support the concepts of identifying performance obligations and the transfer of control of goods or services. Accordingly, the Boards had envisaged that the conclusions about principal versus agent under IFRS 15 could be different in some scenarios from those reached under the previous revenue recognition Standards. Further, the Boards observed that, although exposure to risks and rewards alone does not give an entity control, exposure to risks and rewards can be a helpful factor to consider in determining whether an entity has obtained control.

BC37 The Boards considered whether the indicators in paragraph B37 should be amended to more clearly establish a link between the control principle and the indicators, ultimately deciding to propose the following:

(a) to reframe the indicators as indicators of when an entity controls a specified good or service before transfer, rather than as indicators that an entity does not control the specified good or service before transfer.

(b) to add guidance to explain how each indicator supports the assessment of control as defined in paragraph 33 of IFRS 15. This would help entities apply indicators that are similar to those in previous revenue recognition Standards but within the context of the control principle in IFRS 15.

(c) to remove the indicator relating to the form of the consideration. Although that indicator might sometimes be helpful in assessing whether an entity is an agent, the Boards concluded that it would not be helpful in assessing whether an entity is a principal.

(d) to clarify that the indicators are not an exhaustive list and merely support the assessment of control—they do not replace or override that assessment. Different indicators might provide more persuasive evidence to support the assessment of control in different scenarios.

BC38 In the light of the IASB's decision to generally apply a high hurdle when considering whether to amend IFRS 15, the IASB thought that it would not be necessary to add explanatory text to each indicator in paragraph B37 to establish a link to control. In the IASB's view, clarity about the interaction between the control principle and the indicators could be achieved by amending only the Illustrative Examples. The IASB noted concerns about adding explanatory text to the indicators in paragraph B37 because of (a) the risk of new questions arising with respect to those additional explanations, and (b) the risk that some of those additional explanations might be used inappropriately to reach a principal conclusion when the entity is an agent.

BC39 Nonetheless, despite those concerns, the IASB decided to propose amendments to the indicators in paragraph B37 of IFRS 15 in order to align the wording of the proposed amendments with the wording of those expected to be proposed by the FASB. The IASB concluded that it would be beneficial to propose amendments that would retain converged requirements and guidance on principal versus agent considerations.

The use of the indicators in paragraph B37 rather than the indicators in paragraph 38

BC40 Some stakeholders have questioned why the indicators in paragraph B37 are different from the indicators on the satisfaction of performance obligations (paragraph 38), noting that both sets of indicators relate to control.

BC41 The Boards observed that the indicators in paragraph 38 are indicators of the point in time at which the customer obtains control of the promised good or service. Accordingly, those indicators serve a different purpose than the indicators in paragraph B37. The indicators in paragraph 38 are not intended to indicate whether the customer obtains control of a promised asset—in the context of IFRS 15 as a whole, it is assumed that the customer will obtain control of the promised asset at some point—instead, they are intended to indicate when the customer has obtained control. In contrast, the indicators in paragraph B37 are intended to indicate whether the entity controls a specified good or service at any point before that good or service is transferred to the customer.

Applying control to intangible goods or services

BC42 The Boards observed that at least some of the difficulty that stakeholders had raised about the application of the control principle, in particular to intangible goods and services, is linked to challenges in identifying the specified good or service to be provided to the customer. The Boards observed that this is also frequently a challenge for entities under previous revenue recognition Standards.

BC43 The principal versus agent considerations relate to the application of Step 2 of the revenue recognition model. Appropriately identifying the good or service to be provided is a critical step in appropriately identifying whether the nature of an entity's promise is to act as a principal or an agent. When the appropriate specified good or service is identified, the assessment of control is often relatively straightforward, even in scenarios for which the specified good or service is a virtual or intangible good or service. For example, the specified good or service to be provided to the customer could be:

(a) a right to goods or services (see paragraph 26). For example, the flight ticket (a right to fly) in Example 47 and the meal voucher (a right to a meal) in Example 48 accompanying IFRS 15; or

(b) a bundle of goods or services that are not distinct from each other (for example, the specialised equipment in Example 46 accompanying IFRS 15).

BC44 The Boards observed that when the specified good or service to be provided to the customer is a right to goods or services to be provided in the future by another party, the entity would determine whether its performance obligation is a promise to provide a right to goods or services or whether it is arranging for the other party to provide that right. The fact that the entity will not provide the goods or services itself is not determinative. Instead, the entity evaluates whether it controls the right to goods or services before that right is transferred to the customer. In doing so, it is often relevant to assess whether the right is created only when it is obtained by the customer, or if the right to goods or services exists before the customer obtains the right. If the right does not exist before the customer obtains it, an entity (that is an intermediary) would be unable to control that right before it is transferred to the customer.

BC45 The Boards also observed that the specified good or service to which the control principle is applied should be a distinct good or service, or a distinct bundle of goods or services. If individual goods or services are not distinct from each other, then they are merely inputs to a combined item and are each only part of a single promise to the customer. Accordingly, an entity should evaluate the nature of its promise in the contract (ie to act as a principal or an agent) in the context of the promise to the customer, rather than for part of that promise. Consequently, in contracts in which goods or services provided by another party are inputs to a combined item (or items) for which the customer has contracted, the entity assesses whether it controls the combined item before that item is transferred to the customer.

BC46 When a specified good or service is a distinct bundle of goods or services, the principal versus agent evaluation may, in some cases, be straightforward. The Boards confirmed (in the proposed paragraph B35A(c)) that when an entity provides a significant service of integrating two or more goods or services into a combined output that is the specified good or service for which the customer contracted, it controls that specified good or service before it is transferred to the customer. The entity also controls the goods or services provided by the other party that are inputs to the specified good or service by directing their use to create the combined item. In that case, the inputs provided by the other party would be a fulfilment cost to the entity. In contrast, if a third party provides the significant service of integration, then the entity's customer for its goods or services (which would be inputs to the specified good or service) is likely to be the other party.

BC47 Consequently, the Boards decided to clarify the thought process to be applied when assessing whether an entity is a principal or an agent by specifically requiring an entity to identify the specified good or service before applying the control principle to that specified good or service. The proposed additional paragraph (paragraph B34A) would achieve the following:

(a) it would provide a better framework (ie clarify the thought process) to be applied when assessing whether an entity is a principal or an agent.

(b) it would emphasise the importance of appropriately identifying the specified good or service (which could be a right to a good or service to be provided by another party) that will be transferred to the customer.

(c) it would clarify that the ‘specified good or service’ (ie the unit of account for the principal versus agent evaluation) is each distinct good or service (or distinct bundle of goods or services). Accordingly, it would also clarify that, because a contract with a customer could include more than one specified good or service, an entity could be a principal for one or more specified goods or services in a contract and an agent for others.

(d) it would emphasise that control (as defined in paragraph 33 of IFRS 15) is the determining factor when assessing whether an entity is a principal or an agent.

BC48 The IASB noted that, in many respects, paragraph B34A simply points to other relevant parts of the requirements in IFRS 15. Accordingly, the IASB did not view the inclusion of that additional paragraph as essential to clarifying the requirements in IFRS 15—in its view, clarity about the thought process to be applied could be achieved by amending only the Illustrative Examples. Nonetheless, given the concerns raised by stakeholders, the IASB concluded that the inclusion of paragraph B34A would be helpful to the principal versus agent evaluation, and would align the wording of the proposed amendments with the wording of those expected to be proposed by the FASB. The IASB noted the benefits of proposing amendments that would retain converged requirements and guidance on principal versus agent considerations.

Assessment of control of a service

BC49 The TRG’s discussions highlighted concerns about the application of the control principle to services to be provided to a customer. Questions discussed included how an entity (other than the service provider) could control a service before that service is transferred to the customer because a service comes into existence only at the moment that it is delivered.

BC50 The Boards observed that an entity can control a service to be provided by another party when it controls the right to the specified services from the other party that will be provided to the customer. The entity then either transfers the right to the services to the customer or uses its right to direct the other party to provide the services to the customer on the entity’s behalf (ie to satisfy the entity’s performance obligation in the contract with the customer). Determining whether the entity controls a right to a specified service requires consideration of the facts and circumstances. The Boards noted that contracts involving services provided by another party in which the entity is a principal can be broadly categorised as follows:

(a) Contracts in which an entity provides the customer with a right to a future service to be provided by another party, such as the right to a specified flight (in the form of a ticket) to be provided by an airline (as discussed in paragraph BC44 above).

(b) Contracts in which the service provided by the other party is not distinct from other goods or services promised to the customer, and the entity directs the use of that service to create the combined item that is the specified good or service for which the customer has contracted (as discussed in paragraphs BC45–BC46 above). The proposed paragraph B35A(c) states that this scenario would exist whenever the entity provides a significant service of integrating the service provided by another party into the specified good or service for which the customer has contracted. Example 46 accompanying IFRS 15 illustrates this scenario.

(c) Contracts in which an entity engages (ie directs) another party to provide the service to the customer on the entity's behalf in satisfying the entity's performance obligation. The proposed Example 46A accompanying IFRS 15 illustrates this scenario.

BC51 The Boards observed that determining whether an entity is a principal or an agent is more difficult in the third category of contracts. Having entered into a contract with a customer, the entity engages another party to satisfy a performance obligation within that contract on its behalf. In these contracts, the entity would assess whether it controls a right to the specified services. An entity could control the right to the specified services by entering into a contract with the service provider, and defining the services to be performed by the service provider on the entity's behalf. In that scenario, the entity obtains the right to the services of the service provider, and then directs the service provider to provide the services to the customer on the entity's behalf. This scenario is equivalent to the entity fulfilling the contract using its own resources rather than engaging a service provider to do so. The entity would remain responsible for the satisfactory provision of services in accordance with the contract with the customer. In other scenarios in which the specified services provided to the customer are provided by another party and the entity did not have the ability to direct those services, the entity would typically be an agent. In those scenarios, the entity is likely to be facilitating (and arranging for) the provision of services by the service provider, rather than controlling the rights to the services that the entity then directs to the customer.

BC52 The Boards noted that paragraph B35 explains that an entity that is a principal in a contract may satisfy a performance obligation by itself or it may engage another party to satisfy some or all of a performance obligation on its behalf. The Boards decided to add further explanation to clarify the assessment of control of a service by explaining the scenarios in which a principal can control a service to be provided by another party. The Boards also decided to propose Example 46A accompanying IFRS 15 to illustrate the application of control to services.

Estimating revenue as a principal

BC53 Some TRG participants asked how an entity that is a principal would estimate the amount of revenue to recognise if it were not aware of the amounts being charged to customers by an intermediary that is an agent.

BC54 The IASB observed that this question is largely unrelated to the guidance on principal versus agent considerations in paragraph B34–B38, but rather relates to applying the requirements in paragraphs 46–90 on determining the consideration to which an entity is entitled.

BC55 The IASB concluded that this does not appear to be a significant issue for a number of reasons:

(a) Typically, an entity that is the principal in a transaction (and thus provides promised goods or services to a customer) would know the consideration being paid by the customer to which the entity is entitled. If the entity does not know the consideration to which it is entitled, it might raise a question as to whether the entity's customer is the intermediary in the transaction rather than the end customer (ie the intermediary is a principal in providing the promised good or service to the end customer, and not an agent). Even when an entity (that is a principal) is unaware of amounts being charged to customers, the entity would generally be expected to be able to apply judgement and make estimates about the consideration to which it is entitled using all relevant facts and circumstances available to it.

(b) The situations in which an entity that is a principal may be unaware of the amount charged by an agent to customers are generally limited to situations in which the agent (i) has some flexibility in setting prices or (ii) is procuring the good or service on behalf of the customer:

(i) In situations for which the agent has some flexibility in setting prices, the ability of the agent to charge a different price to customers could be considered to affect only the fee or commission income of the agent. In other words, the agent may be willing to forego a part of its fee or commission in those situations.

(ii) In situations for which the agent is procuring the good or service on behalf of the customer, the net consideration retained by the agent is the fee or commission that the customer pays the agent for arranging for the entity to provide the good or service to the customer. In these cases, the agent is primarily an agent of the customer and the transaction price for the entity is the amount remitted by the intermediary.

BC56 The IASB concluded that the issue does not require any clarifications or additional guidance because the issue is expected to arise only in a narrow set of circumstances.

Licensing

BC57 The TRG discussed issues relating to the application of the licences guidance in IFRS 15. The main issues discussed relate to:

(a) determining the nature of the entity's promise in granting a licence of intellectual property;

(b) the scope and applicability of the sales-based and usage-based royalties exception;

(c) the effect of particular contractual restrictions in a licence on identifying the performance obligations in the contract; and

(d) when the guidance on determining the nature of the entity's promise in granting a licence applies.

BC58 In the light of those discussions and the feedback received, the IASB is proposing to clarify the Application Guidance on licensing and accompanying Illustrative Examples to improve the operability and understandability of the guidance. The IASB thinks that the proposed clarifications do not change the underlying principles of accounting for licences of intellectual property in IFRS 15. In some cases, the IASB has decided that a clarification is not necessary because there is adequate guidance in IFRS 15 with sufficient explanation of the Boards' decisions in the accompanying Basis for Conclusions. The FASB has reached different conclusions about whether and how to address stakeholder concerns.

Determining the nature of the entity's promise in granting a licence of intellectual property

BC59 IFRS 15 specifies criteria in paragraph B58 for determining whether the nature of the entity's promise in granting a licence is to provide a customer with a right to access the entity's intellectual property as it exists throughout the licence period, or a right to use the entity's intellectual property as it exists at a point in time when the licence is granted. In developing IFRS 15, the Boards noted that these criteria were necessary because it is difficult to assess when the customer obtains control of assets in a licence without first identifying the nature of the entity's performance obligation.

BC60 IFRS 15 explains in paragraph B57 that the determination of whether an entity's promise to grant a licence provides a customer with a right to access or a right to use an entity's intellectual property is based on whether the customer can direct the use of, and obtain substantially all of the remaining benefits from, a licence at the point in time at which the licence is granted. A customer can direct the use of, and obtain substantially all the benefits from, the intellectual property, if the intellectual property to which the customer has rights is not significantly affected by activities of the entity. In contrast, a customer cannot direct the use of, and obtain substantially all of the remaining benefits from, a licence at the point in time at which the licence is granted if the intellectual property to which the customer has rights changes throughout the licence period. The intellectual property will change when the entity continues to be involved with its intellectual property and the entity undertakes activities that significantly affect the intellectual property to which the customer has rights. Paragraph B58 provides criteria to help an entity to assess whether its activities 'change' the intellectual property to which the customer has rights, including whether the expected activities of the entity significantly affect the intellectual property to which the customer has rights.

BC61 Stakeholders agree that activities that change the form or functionality of the intellectual property would represent activities that affect the intellectual property to which the customer has rights. However, stakeholders have indicated that it is unclear whether the reference in IFRS 15 to changes in the intellectual property solely refers to changes in the form or functionality of the intellectual property, or also includes changes in the value of the intellectual property. This has resulted in different interpretations about how to apply the criteria in paragraph B58(a). Some stakeholders hold the view that, for activities to significantly affect the intellectual property to which the customer has rights, those activities must be expected to change the form or functionality of that intellectual property. They think that changes that solely affect the value of the intellectual property do not significantly affect the intellectual property to which the customer has rights. Others think that activities that significantly affect the value of the intellectual property are sufficient to conclude that the licence provides a right to access the intellectual property.

BC62 The IASB decided to clarify the requirements of paragraph B58(a) by providing additional guidance on when activities change the intellectual property to which the customer has rights. The IASB noted that the reference to form or functionality in paragraph B61 (and some of the Illustrative Examples and Basis for Conclusions) was not intended to suggest that the nature of a licence is a right to access intellectual property only if the entity's activities significantly affect the form or functionality of the intellectual property to which the customer has rights. Determining the nature of a licence is defined by the criteria in paragraph B58, which do not refer to form or functionality.

BC63 Paragraph B59A proposes to clarify that the assessment of whether the entity's activities change the intellectual property to which the customer has rights is based on whether those activities affect the intellectual property's ability to provide benefit to the customer (ie the 'utility' of the intellectual property). In some cases, the utility of intellectual property is derived from the form or functionality of the intellectual property to which the customer has rights and, in other cases, from the value of that intellectual property. If the activities are expected to change the form or functionality of the intellectual property, those activities are considered to significantly affect the customer's ability to obtain benefit from the intellectual property. If the activities do not change the form or functionality but the ability of the customer to obtain benefit from the intellectual property is substantially derived from, or dependent upon, the entity's activities after the licence is granted, then the activities are also considered to significantly affect the intellectual property (as long as those activities do not result in the transfer of a good or service to the customer). In these cases, it is not necessary for those activities to change the form or functionality of the intellectual property to significantly affect the utility of the intellectual property. This is because, in some circumstances (eg licences of brands), the benefit of the intellectual property is derived from its value and the entity's activities to support or maintain that value.

BC64 The IASB observed that intellectual property that has significant stand-alone functionality derives a substantial portion of its benefit from that functionality. Consequently, if the entity's activities do not change the functionality of such intellectual property, then the entity's activities will not significantly affect the customer's ability to derive benefit from the intellectual property to which the customer has rights. Therefore, the IASB is proposing to clarify that in these cases the criterion in paragraph B58(a) would not be met and the licence would be a right to use intellectual property.

BC65 The IASB is not proposing to define the term 'significant stand-alone functionality' but is proposing clarifications to the Illustrative Examples to demonstrate when the intellectual property to which the customer has rights might have significant stand-alone functionality. In many cases, it will be clear when intellectual property has significant stand-alone functionality. If there is no significant stand-alone functionality, the benefit to the customer might be derived substantially from the value of the intellectual property and the entity's activities to support or maintain that value. The IASB acknowledges, however, that an entity may need to apply judgement to determine whether the intellectual property to which the customer has rights has significant stand-alone functionality. Intellectual property that often has significant stand-alone functionality includes software, biological compounds or drug formulas, and completed media content (for example, films, television shows and music recordings).

BC66 The IASB is also proposing to delete paragraph B57. This is in response to stakeholder concerns that paragraph B57 has contributed to the confusion about whether change solely refers to changes in the form or functionality of intellectual property or also includes changes in the value of intellectual property. The IASB is of the view that the proposed addition of paragraph B59A provides clarity about the intended meaning of change in intellectual property, which makes the detailed discussion in paragraph B57 redundant in the context of the Application Guidance. The discussion in paragraph B57 explains the IASB's basis for its decisions on how to determine whether an entity's promise to grant a licence provides a customer with either a right to access or a right to use an entity's intellectual property. Accordingly, the IASB will incorporate the content of paragraph B57 into the Basis for Conclusions on IFRS 15.

BC67 Having considered the wider implications of amending IFRS 15 at this time (described in paragraph BC3), the IASB decided to clarify the approach to determining the nature of an entity's promise in providing a licence, rather than change that approach. The IASB is of the view that stakeholder concerns can be addressed adequately by providing greater clarity about how to apply the requirements within the Standard. If, as a result of the Standard's post implementation review, a significant change to the requirements is deemed necessary, the IASB will amend IFRS 15. Changing the requirements at this stage creates the risk of unintended consequences and of disrupting the process of implementing the Standard.

Alternative approach proposed by the FASB

BC68 The FASB has proposed an alternative approach to determine whether a licence constitutes a right to access or a right to use based on the nature of the intellectual property. The FASB explained that the basis for this approach is whether an entity's promise to a customer includes supporting or maintaining the intellectual property to which the customer has rights, which in turn largely depends on whether the intellectual property has significant stand-alone functionality.

BC69 The FASB has proposed that intellectual property is either:

(a) functional intellectual property, which is intellectual property that has significant stand-alone functionality and derives a substantial portion of its utility from its significant stand-alone functionality. In this case, a customer generally obtains a licence for the right to use intellectual property unless the functionality of the intellectual property is expected to substantively change during the licence period as a result of activities of the entity that do not transfer a good or service to the customer and the customer is contractually or practically required to use the updated intellectual property; or

(b) symbolic intellectual property, which is intellectual property that does not have significant stand-alone functionality. Substantially all of the utility of symbolic intellectual property is derived from its association with the entity's past or ongoing activities, including its ordinary business activities. In this case, a customer obtains a licence for the right to access intellectual property.

BC70 The FASB's approach looks to the nature of the intellectual property to determine whether activities significantly affect the intellectual property to which the customer has rights. The FASB's proposals have the potential to result in some licences of symbolic intellectual property being classified as a right to access intellectual property, even though there is no expectation that the entity will undertake activities after making the intellectual property available to the customer. Nonetheless, the FASB decided to propose this alternative approach on the basis of feedback that the approach would be more operable than the current approach, particularly for entities with a significant number of licensing arrangements and those with diversified operations. The FASB also observed that it expects the outcomes under this alternative approach to differ from those under the approach within IFRS 15 in relatively few cases. In its view, most licensors continue to be involved with their symbolic intellectual property throughout its economic life.

Consideration in the form of sales-based or usage-based royalties

BC71 Paragraph B63 requires that an entity recognise revenue for a sales-based or usage-based royalty promised in exchange for a licence of intellectual property when the later of the following events occurs: (a) the customer's subsequent sales or usage occurs; and (b) the performance obligation to which some or all of the sales-based or usage-based royalty has been allocated has been satisfied (or partially satisfied). This guidance in paragraph B63 is referred to as the 'royalties constraint'.

BC72 Stakeholders have indicated that it is unclear when a sales-based or usage-based royalty is 'promised in exchange for a licence'. Some stakeholders hold the view that the royalties constraint applies whenever the royalty relates to a licence of intellectual property, regardless of whether the royalty is also consideration for other goods or services in the contract. Other stakeholders have suggested that the royalties constraint applies only when the royalty relates solely to a licence that is distinct in accordance with paragraph 27 or only when the licence is the primary or dominant item to which the royalty relates. Stakeholders have also indicated that it is unclear whether a single sales-based or usage-based royalty should be split into a portion to which the royalties constraint would apply and a portion to which it would not, for example, when the royalty relates to a licence and another good or service that is not a licence.

BC73 In response to stakeholder concerns, the Boards decided to propose to clarify the application of the royalties constraint as follows:

(a) the royalties constraint should apply whenever the predominant item to which the royalty relates is a licence of intellectual property; and

(b) an entity should not split a single royalty into a portion subject to the royalties constraint and a portion that is not (and, therefore, would be subject to the requirements applicable to variable consideration, including the constraint on variable consideration).

Applying the royalties constraint

BC74 The IASB decided to propose in paragraph B63A that the royalties constraint applies to those arrangements for which the licence is the predominant item to which the royalty relates. This is because users of financial statements are likely to view those arrangements as licensing arrangements. The Boards had previously observed in paragraph BC415 of IFRS 15 that it would not be useful for an entity to recognise a minimum amount of revenue for licences of intellectual property for which the consideration is based on the customer's sales or usage. Applying the royalties constraint only when the royalty relates solely to a licence that is distinct in accordance with paragraph 27 might unduly restrict its application.

BC75 The FASB has proposed an example of when a licence is the predominant item to which a royalty relates in paragraph 606-10-55-65A (proposed paragraph B63A of IFRS 15). The IASB decided that no further guidance on the term 'predominant' is necessary because stakeholder feedback suggests that the term can be applied in practice. The IASB acknowledges that judgement is required to determine when a licence is the predominant item to which a sales-based or usage-based royalty relates. However, the judgement and complexity resulting from that determination is likely to be less than that resulting from the application of the general requirements on variable consideration to those arrangements outside the scope of the royalties constraint if the scope were to be more restrictive.

BC76 The IASB decided against expanding the royalties constraint beyond those situations for which a licence is the predominant item to which a royalty relates. This is because doing so would capture arrangements to which the Boards previously concluded that the royalties constraint should not apply (for example, sales of tangible goods that include intellectual property, such as end-user software to which the customer obtains a licence as part of the sale).

BC77 The IASB notes that an entity might conclude that a licence is the predominant item to which a sales-based or usage-based royalty relates when there is more than one performance obligation. This conclusion might be reached regardless of whether the entity concludes that the royalty can be allocated entirely to one performance obligation in accordance with the requirements for allocating variable consideration in paragraphs 84–85. The royalties constraint would also apply when a single licence is not the predominant item to which the royalty relates, but the royalty predominantly relates to two or more licences promised in a contract.

BC78 Through proposed amendments to the Illustrations, the FASB has proposed to clarify how an entity should account for revenue arising from royalties in exchange for a licence that provides a right to access intellectual property (taking into account the requirements on measuring progress towards satisfaction of a performance obligation). The IASB decided not to propose a similar clarification. This is because the amendment illustrates an application of the requirement in paragraph B60 relating to the selection of an appropriate method of measuring progress for performance obligations satisfied over time. The IASB concluded that paragraphs 39–45 and the relevant Application Guidance provide sufficient guidance in this respect.

Splitting a royalty

BC79 Paragraph B63B proposes that an entity should recognise revenue from a sales-based or usage-based royalty entirely in accordance with either the requirement in paragraph B63 (if paragraph B63 applies) or the requirements on variable consideration in paragraphs 50–59 (if paragraph B63 does not apply). The IASB is proposing this clarification in paragraph B63B because the IASB concluded that (a) it would be more complex to account for part of a royalty under the royalties constraint and another part under the general requirements for variable consideration; and (b) doing so would not provide any additional useful information to users of financial statements. This is because splitting a royalty would result in an entity recognising an amount at contract inception that would reflect neither the amount to which the entity expects to be entitled based on its performance, nor the amount to which the entity has become legally entitled during the period.

Contractual restrictions in a licence and the identification of performance obligations

BC80 Some stakeholders suggested that it was unclear whether particular types of contractual restrictions would affect the identification of the promised goods or services in the contract. For example, an arrangement might grant a customer a licence of a well-known television programme or movie for a period of time (for example, three years), but the customer might be restricted to showing that licensed content only once per year during each of those three years. Those stakeholders acknowledged that paragraph B62 is clear that restrictions of time, geography or use do not affect the licensor's determination about whether the licence is satisfied over time or at a point in time. However, in their view, it is unclear whether contractual restrictions affect the entity's identification of its promises in the contract (ie whether the airing restrictions affect whether the entity has granted one licence or three licences).

BC81 Having considered the wider implications of amending IFRS 15 at this time (described in paragraph BC3), the IASB decided that a clarification about the effect of contractual restrictions in licensing arrangements on the identification of the promised goods or services in the contract was not necessary. This is because, in its view, there is adequate guidance in IFRS 15 and the accompanying Basis for Conclusions. Paragraph B62 states that restrictions of time, geographical region or use define the attributes of the promised licence, rather than define whether the entity satisfies its performance obligation at a point in time or over time. Paragraph BC411 of IFRS 15 explains that restrictions 'define attributes of the rights transferred rather than the nature of the underlying intellectual property and the rights provided by the licence', ie the contractual restrictions define the attributes of the licence and do not change the number of promises in the contract. Consequently, the IASB did not intend for a licence to show a movie only on a particular date in each year over a three-year period to be accounted for as three licences.

BC82 In response to stakeholder concerns, the FASB has proposed additional guidance to confirm that contractual restrictions of the nature described in paragraph B62 are attributes of the licence. The restrictions define the scope of the licence and, therefore, do not affect the assessment of the promises in the contract. The FASB also concluded that not all contractual provisions relating to the scope of the licence should be characterised as restrictions of the customer's right under the licence. In the FASB's view, in some cases, the terms of the contract effectively revoke the customer's rights for part of the licence term and, accordingly, the contract contains more than one licence with non-contiguous terms. The FASB has proposed two examples to illustrate when contractual provisions relating to the scope of the licence should be characterised as restrictions of the customer's right and when they revoke a customer's rights under the licence.

When to consider the nature of the entity's promise in granting a licence

BC83 Paragraph B55 requires that an entity apply the general revenue recognition model (paragraphs 31–38) to determine whether a performance obligation that contains a licence that is not distinct (in accordance with paragraph 27) is satisfied at a point in time or over time. Since the issuance of IFRS 15, some stakeholders have questioned when the licensing guidance on determining the nature of an entity's promise applies to a performance obligation that contains a licence and other goods or services. Some hold the view that paragraph B55 suggests that an entity would consider the nature of its promise in granting a licence only when the licence is distinct. Others noted that an entity would have to consider the nature of its promise in granting a licence even when the licence is not distinct to (a) determine whether a combined performance obligation that includes a licence of intellectual property is satisfied over time or at a point in time; and (b) measure progress towards complete satisfaction of that combined performance obligation if it is satisfied over time.

BC84 Again, having considered the wider implications of amending IFRS 15 at this time, the IASB decided that a clarification in this respect is not necessary. IFRS 15 and the explanatory material in the Basis for Conclusions provide adequate guidance to account for a licence that is combined with another good or service. An entity will, however, need to apply judgement to determine the nature of the performance obligation, and to select a method of measuring progress that is consistent with the objective of depicting the entity's performance.

BC85 In making this judgement, the IASB noted that it did not intend for an entity to disregard the guidance on determining the nature of its promise in granting a licence when applying the general revenue recognition model. In some cases, it might be necessary for an entity to consider the nature of its promise in granting a licence even when the licence is not distinct. Paragraph BC407 of IFRS 15 highlights that an entity would consider the nature of its promise in granting the licence if the licence is the primary or dominant component of a combined performance obligation. For example, if an entity grants a 10-year licence that is not distinct from a one-year service arrangement, it would be inappropriate to conclude that the combined performance obligation is satisfied over the one-year service period if the entity's promise were to provide a right to access the entity's intellectual property over a 10-year period if the licence were distinct.

BC86 The FASB has proposed amendments that explicitly state that an entity should consider the nature of its promise in granting a licence when applying the general revenue recognition model to a combined performance obligation that includes a licence and other goods or services (ie when applying the requirements in Topic 606 equivalent to those set out in paragraphs 31–45).

Other amendments expected to be proposed by the FASB

Collectability and contract termination (paragraphs 9(e) and 15)

BC87 The TRG discussed an implementation question raised by stakeholders about how to apply the collectability criterion in paragraph 9(e) in instances in which the entity has received non-refundable consideration from a customer with poor credit quality. The discussion informed the Boards that there are potentially different interpretations of:

(a) how to apply the collectability guidance in paragraph 9(e) when it is not probable that the total consideration promised in the contract is collectable; and

(b) when to recognise revenue in accordance with paragraph 15 for non-refundable consideration received from the customer when the contract does not meet the criteria in paragraph 9.

Assessing collectability

BC88 Paragraph 9(e) requires an entity to assess whether it is probable that it will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. This assessment forms part of Step 1 of IFRS 15 *Identify the contract(s) with a customer*.

BC89 The TRG's discussions informed the Boards that some stakeholders interpret this guidance to mean that an entity should assess the probability of collecting all of the consideration promised in the contract. Under this interpretation, some contracts with customers that have poor credit quality would not meet the criteria in paragraph 9(e), even though they are otherwise valid and genuine contracts. Other stakeholders assert that those contracts would be valid and genuine if the entity has the ability to protect itself from credit risk.

BC90 The Boards noted that the assessment in paragraph 9(e) requires an entity to consider the relative position of the entity's contractual rights to the consideration and the entity's performance obligations. That assessment considers the entity's exposure to the customer's credit risk and the business practices available to the entity to manage its exposure to credit risk throughout the contract. For example, an entity may be able to stop providing goods or services to the customer or require advance payments. This is consistent with the explanation of the Boards' considerations as described in paragraph BC46 of IFRS 15—that paragraph states that, if the customer were to fail to perform as promised and consequently the entity would respond to the customer's actions by not transferring any further goods or services to the customer, the entity would not consider the likelihood of payment for those goods or services that would not be transferred.

BC91 Having considered the wider implications of amending IFRS 15 at this time, the IASB concluded that the existing guidance in IFRS 15 and the explanatory material in the Basis for Conclusions are sufficient. The IASB noted that it expects practice to develop consistently with the Boards' intentions in developing the collectability criterion in paragraph 9(e). The IASB also would not have expected any possible clarifications to paragraph 9(e) to result in practical differences in reporting outcomes.

BC92 In reaching its decision, the IASB observed that an entity will generally not enter into a contract with a customer if the entity does not consider it to be probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. This is consistent with the Boards' reasoning in paragraph BC43 of IFRS 15, which states that entities generally only enter into contracts for which it is probable that the entity will collect the amount to which it will be entitled. It was not the Boards' intention that many contracts should fail the condition in paragraph 9(e). On this basis, the IASB thinks that the population of contracts to which any clarification to paragraph 9(e) might apply is small.

BC93 The FASB decided to propose amendments to the implementation guidance and Illustrations in Topic 606 that clarify how an entity should assess collectability in Step 1 of the revenue recognition model. The amendments are expected to confirm that the collectability assessment may be based on a portion of the consideration promised in the contract to which it will be entitled in exchange for the goods or services that will be transferred to the customer.

Contract termination

BC94 Paragraph 15 specifies when consideration received from a customer should be recognised as revenue by an entity that has failed Step 1 of the revenue recognition model. Paragraph 15(b) states that revenue should be recognised when the contract has been terminated and the consideration received from the customer is non-refundable.

BC95 The TRG's discussions informed the Boards about potential diversity in stakeholders' understanding of when a contract is terminated. The assessment of when a contract is terminated affects when an entity recognises revenue in a contract that does not meet Step 1 of the revenue recognition model. Some stakeholders assert that a contract is terminated when an entity stops transferring promised goods or services to the customer. Other stakeholders assert that a contract is terminated only when the entity stops pursuing collection from the customer. Stakeholders noted that those two events often occur at different points in time. For example, entities sometimes pursue collection for a significant period of time after they have stopped transferring promised goods or services to the customer. As a result, non-refundable consideration received from the customer might be recognised as a liability for a significant period of time during which an entity pursues collection, even though the entity may have stopped transferring promised goods or services to the customer and has no further obligations to transfer goods or services to the customer.

BC96 The IASB noted that contracts often specify that an entity has the right to terminate the contract in the event of non-payment by the customer and that this would not generally affect the entity's rights to recover any amounts owed by the customer. The IASB also noted that an entity's decision to stop pursuing collection would not typically affect the entity's rights and the customer's obligations under the contract with respect to the consideration owed by the customer. On this basis, the IASB concluded that the existing guidance in IFRS 15 is sufficient for an entity to conclude that a contract is terminated when it stops providing goods or services to the customer without any additional clarification. Some IASB members also expressed concerns about the potential for unintended consequences relating to other areas of IFRS if contract termination were to be defined in IFRS 15. Consequently, the IASB decided not to propose any amendments relating to paragraph 15.

BC97 The FASB decided to propose amendments that clarify when a contract is terminated in accordance with paragraph 606-10-25-7 (paragraph 15 of IFRS 15).

Non-cash consideration

BC98 The TRG discussed the following implementation questions raised by stakeholders in connection with applying IFRS 15 to contracts that involve non-cash consideration:

(a) At which date should the fair value of non-cash consideration be measured in determining the transaction price?

(b) How should the constraint on variable consideration be applied to transactions for which the fair value of non-cash consideration might vary due to both the form of the consideration and for reasons other than the form of consideration?

BC99 Paragraph 66 requires non-cash consideration to be measured at fair value (or by reference to the stand-alone selling price of the goods or services promised to the customer if an entity cannot reasonably estimate fair value). The TRG's discussion informed the Boards that the measurement date for non-cash consideration is unclear and could be interpreted as one of several dates: (a) at contract inception; (b) when the non-cash consideration is received; or (c) at the earlier of when the non-cash consideration is received and when the related performance obligation is satisfied.

BC100 In its discussions, the IASB observed that this issue has important interactions with other Standards (including IFRS 2 *Share-based Payment* and IAS 21 *The Effects of Changes in Foreign Exchange Rates*) and, thus, any decisions made would create a risk of potential unintended consequences. Accordingly, the IASB decided that, if needed, issues relating to the measurement of non-cash consideration should be considered more comprehensively in a separate project.

BC101 The FASB decided to propose an amendment to the guidance in Topic 606 requiring that non-cash consideration should be measured at contract inception. In the FASB's view, measuring non-cash consideration at contract inception is most consistent with the requirements in Topic 606 on determining the transaction price and on allocating the transaction price to performance obligations. The FASB also expects this approach typically to be less costly and less complex to apply in practice than other alternatives.

BC102 The IASB acknowledges that, because it is not proposing a change equivalent to that expected to be proposed by the FASB, the use of a measurement date other than contract inception would not be precluded under IFRS. Consequently, it is possible that diversity between IFRS and US GAAP entities could arise in practice. The IASB observed that, unlike US GAAP, existing IFRS does not contain any specific requirements about the measurement date for non-cash consideration for revenue transactions. Therefore, IFRS 15 is not expected to create more diversity than presently exists in respect of this issue. In addition, discussions with some stakeholders highlighted that any practical effect of different measurement dates would arise in only limited circumstances. The IASB also noted that, if significant, an entity would be required to disclose the accounting policy applied.

BC103 The FASB also decided to propose an amendment clarifying that the constraint on variable consideration applies only to variability that arises for reasons other than the form of the consideration. The requirements in paragraph 68 indicate that the constraint on variable consideration is applied if the fair value of the non-cash consideration promised by a customer varies for reasons other than only the form of the consideration (for example, a change in the exercise price of a share option because of the entity's performance). Since the issuance of IFRS 15, some stakeholders observed that it is not clear whether the variable consideration requirements in paragraphs 56–58 applies in circumstances for which the fair value of non-cash consideration varies due to both the form of the consideration and for reasons other than the form of consideration. In particular, some stakeholders raised concerns that bifurcating the effects of variability might be challenging in some circumstances.

BC104 FASB members observed that applying the variable consideration requirements to both forms of variability might not provide users of financial statements with useful information because the timing of revenue recognition might differ for similar transactions settled in different forms of consideration (for example, cash and shares). Additionally, the inclusion of a minor performance condition could significantly affect the amount of non-cash consideration that would be subject to the constraint on variable consideration. The IASB noted these views but, for reasons discussed in paragraph BC102, decided not to propose an amendment to IFRS 15 for this issue.

Presentation of sales taxes

BC105 Paragraph 47 specifies that amounts collected on behalf of third parties, such as some sales taxes, are excluded from the determination of the transaction price. Entities are therefore required to identify and assess sales taxes to determine whether to include or exclude those taxes from the transaction price.

BC106 Since the issuance of the new revenue Standard, some US stakeholders have expressed concerns about the cost and complexity of assessing tax laws in each jurisdiction because many entities operate in numerous jurisdictions, and the laws in some jurisdictions are unclear about which party to the transaction is primarily obligated for payment of the taxes. These stakeholders also stated that the variation of, and changes in, tax laws among jurisdictions contributes to that complexity. Therefore, some preparers and practitioners requested that the Boards amend the new revenue Standard to add a practical expedient to reduce the complexity and practical difficulties in assessing whether a sales tax is collected on behalf of a third party.

BC107 The FASB decided to propose a practical expedient that permits an entity to exclude from the measurement of the transaction price all taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction and collected from customers (for example, sales, use, value added and some excise taxes). Taxes assessed on gross receipts or imposed during the inventory procurement process are expected to be excluded from the scope of the election. The scope of the election is expected to be based on guidance in previous revenue Standards under US GAAP.

BC108 The IASB is not proposing to add a similar practical expedient to IFRS 15 for the following reasons:

(a) it would reduce the comparability of revenue between entities under different tax regimes in different jurisdictions, as well as entities in the same jurisdictions to the extent that they elect different approaches.

(b) the previous revenue recognition Standards under IFRS contained requirements applicable to sales tax similar to those in IFRS 15. Therefore assessing whether sales taxes are collected on behalf of a third party is not a new requirement for IFRS preparers.

(c) it would create an exception to the revenue recognition model that does not reflect the economics of the arrangement in cases for which a sales (or similar) tax is a tax on the entity rather than a tax collected by the entity from the customer on behalf of a tax authority.

Practical expedients on transition

BC109 Paragraph C3 specifies that the requirements in IFRS 15 should be applied either (a) retrospectively to each reporting period presented with restatement of comparative periods (the full retrospective method); or (b) retrospectively with the cumulative effect of initially applying the guidance recognised at the date of initial application (the modified retrospective method). Paragraphs 18–21 specify the accounting for contract modifications.

BC110 Since the issuance of IFRS 15, stakeholders have raised concerns relating to potential challenges in applying the transition requirements in IFRS 15 to (a) contracts that have been modified before the date of initial application; or (b) contracts for which the entity has transferred all of the goods or services identified in accordance with IAS 11 *Construction Contracts* or IAS 18 (ie completed contracts as defined in IFRS 15).

Modified contracts

BC111 The IASB decided to propose a practical expedient on transition that would allow an entity to reflect the aggregate effect of all of the modifications that occurred between contract inception and the earliest date presented when identifying performance obligations and determining the transaction price, rather than accounting for the effects of each modification separately. This would permit an entity to apply hindsight at the beginning of the earliest period presented in accounting for contract modifications that occurred before that date. The IASB thinks that this approach would provide some cost relief and yet would result in financial information that closely aligns with the financial information that would be available under IFRS 15 without the expedient. The FASB also decided to propose a similar practical expedient.

BC112 The IASB is proposing that all entities should apply the expedient at the beginning of the earliest period presented so that entities electing the modified retrospective method do not have to wait until the date of initial application before finalising the accounting for previous modifications. The FASB decided to propose that entities should apply the expedient at the beginning of the earliest period presented in accordance with Topic 606. For entities electing the full retrospective method, this would be on the same basis as the IASB's decisions. However, for entities electing the modified retrospective method, this would be the date of initial application of Topic 606.

BC113 The Boards considered, but rejected, permitting an entity to account for the unsatisfied performance obligations in a modified contract at transition as if the original contract were terminated and a new contract created as of the transition date. This would eliminate the need to evaluate the effects of modifications before transition. Under this approach, the amount of consideration allocated to the unsatisfied performance obligations would be the total consideration promised by the customer (including amounts already received) less any amounts previously recognised as revenue under previous revenue Standards. Although this might significantly reduce the cost and complexity of applying the transition requirements to contract modifications, the approach was rejected by both Boards because it could result in financial information that differed significantly from that under IFRS 15 without the expedient.

Completed contracts

BC114 The Boards discussed a further possible practical expedient to permit an entity electing the full retrospective method not to apply the Standard to contracts that are completed contracts as defined as of the beginning of the earliest period presented. The IASB decided to propose amendments to introduce this practical expedient. The IASB noted that reducing the population of contracts to which IFRS 15 applies (the consequence of applying this practical expedient) could significantly reduce the effort and cost of initial application. In addition, the IASB observed that a similar expedient is currently given to first-time adopters in paragraph D35 of IFRS 1 *First-time Adoption of International Financial Reporting Standards*.

BC115 The FASB decided not to propose a similar expedient to the transition guidance because it concluded that application of such an expedient would not faithfully depict a full retrospective application of Topic 606. The IASB acknowledged that the expedient could affect the comparability of financial information under the full retrospective method, but concluded that this would be outweighed by the benefit provided by the reduced transition costs.

Transition and effective date

BC116 The IASB is not proposing an effective date for *Clarifications to IFRS 15*. The IASB's objective is to finalise the proposed amendments with sufficient time to set an effective date that aligns with the revised effective date of IFRS 15. In July 2015, the IASB decided to defer the effective date of IFRS 15 by one year to 1 January 2018.

BC117 The IASB proposes to allow early application of *Clarifications to IFRS 15*. Therefore, an entity that chooses to apply IFRS 15 before its effective date would be permitted to apply IFRS 15 as amended by these clarifications. However, that entity would also be permitted to apply the clarifications at a date later than when it first applies IFRS 15.

BC118 The IASB proposes that an entity should apply the proposed amendments retrospectively in accordance with IAS 8. In reaching its decision to require retrospective application, the IASB observed that the amendments are intended to clarify the IASB's intentions when developing the requirements in IFRS 15 rather than change the requirements of IFRS 15. The IASB decided not to propose prospective application of *Clarifications to IFRS 15* because this would reduce comparability in the limited cases that the proposed amendments may result in significant changes to an entity's application of IFRS 15. This approach is consistent with feedback received from users of financial statements during the development of IFRS 15 highlighting that retrospective application would be the most useful transition method for them to understand trends in revenue.

BC119 Paragraph C8A proposes that in applying the amendments retrospectively, an entity should apply the amendments as if they had been included in IFRS 15 at the date of initial application. The expected outcome of applying the amendments retrospectively is summarised as follows:

(a) for entities that adopt both IFRS 15 and *Clarifications to IFRS 15* at the same time, any effect of applying the amendments would be reflected in the effects of initially applying IFRS 15.

(b) for entities that adopt *Clarifications to IFRS 15* after the date of initial application of IFRS 15, the effects of initially applying IFRS 15 would be restated for the effects, if any, of initially applying the amendments.

BC120 The outcome of retrospective application of *Clarifications to IFRS 15* will depend on which transition method an entity selects when it first applies IFRS 15—either the full retrospective method or the modified retrospective method. The selection of the transition method will determine, for example, whether periods before the date of initial application of IFRS 15 are restated as well as the amount and date of the adjustment to retained earnings. Retrospective application of *Clarifications to IFRS 15* will affect only those reporting periods and those contracts to which IFRS 15 has been applied. For example, consider an entity that uses the modified retrospective method and initially applies IFRS 15 on 1 January 2017 and *Clarifications to IFRS 15* on 1 January 2018. Retrospective application of *Clarifications to IFRS 15* would not require the restatement of financial information before 1 January 2017 for the effects of the amendments. Any effect of applying the amendments would be included in a restated cumulative effect adjustment as of 1 January 2017.

Alternative view

Alternative view on the Exposure Draft *Clarifications to IFRS 15* as published in July 2015

AV1 Mr Ochi voted against the publication of the Exposure Draft *Clarifications to IFRS 15*. He agrees with all of the proposed clarifying amendments to IFRS 15 and the additional transition reliefs. However, he disagrees with the proposal to require an entity to apply the amendments to IFRS 15 retrospectively. Mr Ochi thinks that the IASB should propose a different transition method for those entities that apply the amendments at a date later than when they first apply IFRS 15 as originally issued. Specifically, he thinks such entities should be permitted to apply the amendments to IFRS 15 prospectively, ie only to contracts entered into on or after the effective date of the amendments.

AV2 Mr Ochi notes that the IASB allowed early application of IFRS 15 and acknowledges that many entities might be well advanced in their implementation processes. Indeed, he is aware of at least one large company that has already adopted IFRS 15. Consequently, some entities might in effect be required to restate some contracts twice, both on first applying IFRS 15 as originally issued and again when first applying the amendments to the Standard.

AV3 Mr Ochi agrees in principle with publishing clarifications to a Standard before the effective date of that Standard if they would be helpful to constituents. However, in such cases, he thinks that the IASB should provide due consideration to those entities that have already started to prepare for early application of the Standard. Mr Ochi notes that a number of jurisdictions are at different stages in their adoption of IFRS. In that regard, he thinks that allowing early application of a Standard supports the smooth adoption of IFRS. He therefore believes that the IASB should be careful to ensure that it does not in effect penalise those entities that begin their implementation process early and reward those that delay. Mr Ochi thinks it is not just a question of considering the extent or potential effect of any clarifications to a Standard; rather it is a matter of principle. Mr Ochi thinks that proposing clarifications, even if their potential effect is expected to be limited, could adversely affect the behaviour of entities in the future when the IASB issues new Standards. This might act as a disincentive to entities to start their implementation of a new Standard on a timely basis.

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