Ernst & Young
8 Exhibition Street
Melbourne VIC 3000 Australia
GPO Box 67 Melbourne VIC 3001

Tel: +61 3 9288 8000
Fax: +61 3 8650 7777
ey.com/au

The Chair
Australian Accounting Standards Board
PO Box 204
Collins St West
VIC 8007
Australia

30 October 2015

Dear Ms Peach

Ernst & Young's global submissions to the IASB

Please find enclosed Ernst & Young's global submissions to the IASB on the following exposure drafts:

- **Exposure Draft ED/2015/5** – *Remeasurement on a Plan Amendment, Curtailment or Settlement/Availability of a Refund from a Defined Benefit Plan – Proposed amendments to IAS 19 and IFRIC 14*
- **Exposure Draft ED/2015/7** - *Effective Date of Amendments to IFRS 10 and IAS 28*
- **Exposure Draft ED/2015/6** – *Clarifications to IFRS 15*

Yours sincerely

Ernst & Young

Ernst & Young

Encl:

Ernst & Young Global Limited
Becket House
1 Lambeth Palace Road
London
SE1 7EU

Tel: +44 [0]20 7980 0000
Fax: +44 [0]20 7980 0275
ey.com

International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH
United Kingdom

19 October 2015

Dear Board members,

Invitation to comment – Exposure Draft ED/2015/5 – Remeasurement on a Plan Amendment, Curtailment or Settlement/Availability of a Refund from a Defined Benefit Plan – Proposed amendments to IAS 19 and IFRIC 14 (ED)

Ernst & Young Global Limited, the central coordinating entity of the global EY organisation, welcomes the opportunity to offer its views on Exposure Draft ED/2015/5 – *Remeasurement on a Plan Amendment, Curtailment or Settlement/Availability of a Refund from a Defined Benefit Plan (Proposed amendments to IAS 19 and IFRIC 14)* issued by the International Accounting Standards Board (IASB or Board) in June 2015.

Overall, we support the fact that the IASB is addressing the topics identified in the ED. Our principal comments on the proposals are set out later in this letter. Our detailed responses to the specific questions asked in the ED are given in Appendix A. In summary, regarding Question 1, we do not support the respective amendments, as proposed, nor the direction of these proposed amendments. Regarding Questions 2, 3, 4 and 5, overall we agree with the amendments proposed, but we have some concerns about the wording of specific amendments.

Before providing our detailed comments on the ED, we would like to briefly highlight our overarching observations on the requirements of IAS 19 which have led us to raise a number of the questions with the Board.

Market transactions (such as 'buy-outs', 'buy-ins' and longevity swaps) as well as on-going funding requirements have shown that in many instances the actual funding obligation is higher than the recognised IAS 19 defined benefit obligation . As reflected in the examples in IFRIC 14, this raises questions of how to assess the recoverability of any asset recognised for an accounting surplus when the practical reality is that there is no surplus, but only cash outflows to make good a funding deficit. In our view, the long-term solution to these issues lies in addressing the measurement of the defined benefit obligation (DBO), rather than extending the guidance for a hypothetical recovery of an accounting asset. However, we realise that this would go beyond the scope of the current ED.

In the remainder of this letter and Appendix A, we discuss the proposals in the ED.

1. Availability of a refund from a defined benefit plan

We do not support the proposed amendment because we believe that the fact that a surplus that exists at the reporting date could be extinguished by uncertain future events as a result of decisions by other parties, is not relevant when assessing the existence of an entity's unconditional right to a surplus at the reporting date. Commonly, the trustees of a pension fund will be independent of the entity and will have absolute discretion when deciding on the investment strategy, asset allocation, and whether to buy annuities or settle liabilities. These powers would allow the trustees to 'spend' any current or future surplus and, in our view, such trustee powers should not, of themselves, preclude the recognition of a surplus.

Although it could be argued that a surplus cannot be recognised as an asset if the employer does not control its use (as this would conceptually seem to contradict the definition of an asset as a resource *controlled* by the entity), we believe that considering future events in assessing whether and how to recognise a surplus at the reporting date would be inconsistent with the calculation of the net defined benefit obligation at the reporting date. We note that this is also supported by BC10, BC22 and BC23 of IFRIC 14 which state that, when developing IFRIC 14, the IFRIC agreed that increases or improvements in the benefits provided by the plan should not be anticipated. However, in case the Board wishes to proceed with the proposed amendments, we believe that BC10, BC22 and BC23 of IFRIC 14 would need to be reconsidered as they are not consistent with the concept of the proposed amendments.

Moreover, should the Board wish to proceed with the proposed amendments, we have concerns with the way specific changes have been proposed in the ED:

- While proposed paragraphs 12A and 12C relate to the impact of other parties' powers in respect of the *existence* of a reporting entity's right to a refund of a surplus, it is not clear why proposed paragraph 12B relates to the impact of other parties' powers regarding the *measurement* (rather than existence) of a reporting entity's right to a refund of surplus. We believe that all three conditions described in the proposed paragraphs 12A, 12B and 12C would influence the existence of the surplus. Additionally, we believe that all three conditions could potentially influence the amount of a refund of a surplus that will be available to the reporting entity at a future date. We encourage the Board to be more explicit as to how an entity should make the split between the existence of a right to a refund (recognition) and the measurement of the refund asset.
- What is described in proposed paragraphs 12A, 12B and 12C relates only to specific powers of the other parties (e.g., the trustees). For example, proposed paragraph 12A only relates to the existence of an unconditional right to a refund assuming the gradual settlement of the plan (paragraph 11(b) of IFRIC 14), while it is not clear why the

proposed amendment would not be equally applicable to a right of refund during the life of a plan, as referred to in paragraph 11(a) of IFRIC 14.

- In practice, many of the trustees' powers are contingent on the occurrence of future events outside their control. Therefore, the effect of the second sentence in proposed paragraph 12A may be to make the restriction on recognition of the right to a refund asset meaningless in its entirety, in the sense that the other parties' contingent powers will not actually affect the unconditional right of the entity.
- Proposed paragraph 12C seems inconsistent with proposed paragraph 12A. In particular, it is not clear why a surplus cannot be recognised when trustees can "spend" any current or future surplus in a wind-up without the entity's consent (paragraph 12A), while a surplus can be recognised when trustees have the power to acquire annuities in a buy-in or buy-out arrangement (paragraph 12C).
- The term 'other parties' is used throughout proposed paragraphs 12A, 12B and 12C, but it is not clear who the 'other parties' could be, if not the trustees of the plan.
- In practice, plan assets may be jointly controlled by an entity and other parties. We encourage the Board to clarify whether the proposed amendments would be also applied to such cases.

A more detailed response, including some additional areas of comment, is provided in Appendix A to this document.

2. Remeasurement on a plan amendment, curtailment or settlement

Overall, we agree with and support the proposed amendment. However, we believe that the wording in this amendment may result in some misunderstandings. We encourage the Board to be more explicit as to the determination of the prior period cost by aligning the language used in the definition of past service costs in paragraph 8 and the proposed paragraphs 99A of IAS 19, as well as BC15 to the proposed amendments.

We also urge the Board to clarify the accounting treatment of an asset ceiling upon settlement of a plan that is in surplus (plan assets of the defined benefit pension plan exceed the defined benefit obligation), but this surplus was previously not recognised as a result of the asset ceiling.

As an additional observation, we note that the Board decided not to address the accounting in IAS 19 when "significant market fluctuations" lead to a remeasurement of the net defined benefit obligation for reasons other than a plan amendment, curtailment or settlement. We encourage the Board to address the issue of the potential mismatch between IAS 19 and IAS 34, specifically, whether a remeasurement in situations of "significant market fluctuations" would be prohibited or allowed.

A more detailed response, including some additional areas of comment, is provided in Appendix A to this document.

Should you wish to discuss the contents of this letter with us, please contact Leo van der Tas on +44 (0)20 7951 3152.

Yours faithfully

Ernst & Young Global Limited

Appendix A

Question 1 - Accounting when other parties can wind up a plan or affect benefits for plan members without an entity's consent
The IASB proposes amending IFRIC 14 to require that, when an entity determines the availability of a refund from a defined benefit plan: (a) the amount of the surplus that an entity recognises as an asset on the basis of a future refund should not include amounts that other parties (for example, the plan trustees) can use for other purposes (for example, to enhance benefits for plan members) without the entity's consent. (b) an entity should not assume a gradual settlement of the plan as the justification for the recognition of an asset, if other parties can wind up the plan without the entity's consent. (c) other parties' power to buy annuities as plan assets or make other investment decisions without changing the benefits for plan members does not affect the availability of a refund. Do you agree with the proposed amendments? Why or why not?

Response:

We believe that the fact that a surplus existing at the reporting date could be extinguished by uncertain future events as a result of decisions by other parties is not relevant when assessing the existence of an entity's unconditional right to a surplus at the reporting date. Therefore, we do not support the respective amendments as proposed in this ED and we are concerned about the way they have been proposed in paragraphs 12A and 12B. While we support the amendments that have been proposed in paragraph 12C, we have identified an inconsistency between proposed paragraph 12A and 12C,in particular:

Gradual settlement of the plan as the justification for the recognition of an asset, if other parties can wind up the plan without the entity's consent (paragraph 12A)
On our reading of proposed paragraph 12A it would seem that an entity does not have an unconditional right to a refund where other parties may wind up the plan without the entity's consent, because a refund may not be received if such a wind-up occurs.

In our view, trustees will commonly have absolute discretion to set investment strategy and asset allocation that would allow them to 'spend' any current or future surplus. Such trustee powers should not, of themselves, preclude the recognition of a surplus and, likewise, the fact that a wind-up may occur in the future does not mean that the entity does not have a current unconditional right. The reason for our view is that we see the guidance in IFRIC 14 as relating to whether the entity has an unconditional right to any

Question 1 - Accounting when other parties can wind up a plan or affect benefits for plan members without an entity's consent

surplus that may happen to exist at any future date. It is not concerned with whether such a surplus will exist, or with the powers of others to influence that. We believe that the fact that any surplus could be extinguished by uncertain future events not controlled by the employer is not relevant – it is the right to a surplus, not the existence of a surplus, which is relevant.

Moreover, although it could be argued that a surplus should not be recognised if the entity does not control its use in its capacity as a resource controlled by the entity, we believe that the recognition of an asset to the extent a surplus exists at the end of the reporting period is consistent with the measurement of the net defined benefit obligation at that date and therefore, should be recognised.

IFRIC 14 makes our above arguments clear for future actuarial losses and benefit improvements made by the employer (BC10) and for increases in the size of the workforce or benefits provided by the plan (BC22 and BC23). Our view is that the same applies to asset allocation decisions (including wind-ups), whether decided by the employer or the trustees. This view is further supported by the general requirements in IAS 19 surrounding settlements which are accounted for only when they happen, and this is so whether the decision to settle is taken by the employer or by the trustees. We note that the measurement of a surplus should follow the 'normal' IAS 19 methodology, unless this amendment attempts to establish another measurement basis for which we will need further explanation as we indicate below. However, should the Board wish to proceed with the proposed amendments, we believe that BC10, B22 and BC23 will need to be reconsidered and amended according to the concept of the proposed amendments.

We also note that the second sentence included in proposed paragraph 12A clarifies that any powers of other parties that are contingent on uncertain future events should not be taken into consideration as affecting the entity's right to a refund. Unless other parties' powers are contingent, the entity should be considered as not having an unconditional right. In practice, many of the trustees' powers are contingent on the occurrence of future events outside their control (e.g., regulatory approval, occurrence of a regulatory deficit/surplus, bankruptcy of the employer sponsor). Therefore, the effect of the second sentence in proposed paragraph 12A may be to make the restriction on recognition of the right to a refund asset meaningless in its entirety, in the sense that the other parties' contingent powers will not actually affect the unconditional right of the entity. In that case, proposed paragraph 12A leads in substance to the same conclusion as our view described above where we consider as irrelevant the fact that any surplus could be extinguished by uncertain future events not controlled by the employer.

Question 1 - Accounting when other parties can wind up a plan or affect benefits for plan members without an entity's consent

Amount of surplus recognised as an asset should not include amounts that other parties can use for other purposes without the entity's consent (paragraph 12B)

On one hand, proposed paragraph 12B clarifies the impact of the powers of other parties on the measurement of the surplus when an unconditional right to use some of the surplus resides with those other parties. Proposed paragraphs 12A and 12C, on the other hand, clarify the impact of the powers of other parties on the existence of the reporting entity's unconditional right to a refund of a surplus. We would therefore expect to see paragraph 12B under the section, 'Measurement of the economic benefit' instead of 'The right to a refund'.

Other parties' power to buy annuities as plan assets or make other investment decisions without changing the benefits for plan members (paragraph 12C)

We are in agreement with this condition. However, we believe that there is an inconsistency between proposed paragraphs 12A and 12C as it is not clear why a surplus cannot be recognised if other parties can wind up the plan without the entity's consent (paragraph 12A), while a surplus can be recognised when other parties have the power to use that surplus to acquire annuities in a buy-in or buy-out arrangement. We encourage the Board to address this inconsistency between proposed paragraphs 12A and 12C.

In addition to the above, we would like to comment on the fact that our understanding of IFRIC 14 is that it provides guidance for determining the existence of an unconditional right to a refund, instead of describing how this refund should be initially measured. However, proposed paragraphs 12A, 12B and 12C of IFRIC 14 contain guidance relating to determining the existence of the right to a refund and the measurement of the refund asset. Therefore, before finalising the proposed amendments, we urge the IASB to consider the following:

- Clarifying the guidance that should be followed by an entity, firstly, when assessing the existence of an unconditional right to a refund and secondly when measuring the asset arising from this unconditional right
- Regarding measurement, clarifying whether IAS 19 requirements should be followed when measuring a defined benefit asset or whether the proposed amendments in IFRIC 14 create another measurement basis for the asset would be useful
- Although we support the measurement restrictions in the amount of surplus that a reporting entity recognises on the basis of a future refund proposed in paragraph 12B, we believe that the conditions described in proposed paragraphs 12A and 12C of IFRIC 14 could also potentially affect the amount of refund that will be available to the

Question 1 - Accounting when other parties can wind up a plan or affect benefits for plan members without an entity's consent

reporting entity at a future date. Also, proposed paragraph 12B which refers to the measurement of the amount of surplus (as opposed to proposed paragraphs 12A and 12C), could potentially affect the assessment of the existence of an unconditional right to a refund.

- Proposed paragraphs 12A, 12B and 12C relate only to specific powers of the other parties (e.g., the trustees). It could be implied that any other powers to enhance benefits for plan members or wind up a plan (buy-in or buy-out rights) might be treated in a dissimilar way, although, potentially, they are economically the same. For example, proposed paragraph 12A is only referring to a gradual settlement described in paragraph 11(b) of IFRIC 14, but it is not clear why paragraph 12A would not be equally applicable to a right of refund during the life of the plan in paragraph 11(a). We, therefore, encourage the Board to consider clarifying the impact of other powers held by trustees or other parties (other than those described in proposed paragraphs 12A, 12B and 12C) before concluding on the proposed amendments, in order to avoid dissimilar accounting treatments.
- The term 'other parties' is used throughout proposed paragraphs 12A, 12B and 12C. However, a clarification is needed regarding who the 'other parties' could be, if not the trustees of the plan.
- In practice, defined benefit plans may be jointly controlled by the entity and other parties. Both the entity and other parties may have powers over the plan and the right to a refund of a surplus may depend on the occurrence or non-occurrence of one or more uncertain future events not wholly within an entity's or the other parties' control. The Board should, therefore, address whether the proposed amendments would also apply to such situations.

Question 2 - Statutory requirements that an entity should consider to determine the economic benefit available

The IASB proposes amending IFRIC 14 to confirm that when an entity determines the availability of a refund and a reduction in future contributions, the entity should take into account the statutory requirements that are substantively enacted, as well as the terms and conditions that are contractually agreed and any constructive obligations.

Do you agree with that proposal? Why or why not?

Response:

Yes, overall we agree and support this amendment as we believe that clarifying that an

Question 2 - Statutory requirements that an entity should consider to determine the economic benefit available

entity should take into account the statutory requirements that are substantively enacted, as well as the terms and conditions that are contractually agreed and any constructive obligations, is helpful in eliminating an area of diversity in current practice.

In addition, according to BC8 of the proposed amendments, we note that one of the purposes of this amendment is to achieve consistency with the requirements of paragraph 88 of IAS 19 which relates to the defined benefit obligation. We, therefore, encourage the Board to also amend paragraph 88 of IAS 19 by using the same wording with proposed amended paragraph 7 of IFRIC 14. We suggest the following revisions to paragraph 88 of IAS 19:

> *"88 Actuarial assumptions reflect future benefit changes that are set out in the formal terms of a plan (or a constructive obligation that goes beyond those terms) that are enacted or substantively enacted, at the end of the reporting period…"*

Question 3 - Interaction between the asset ceiling and past service cost or a gain or loss on settlement

The IASB proposes amending IAS 19 to clarify that:

(a) the past service cost or the gain or loss on settlement is measured and recognised in profit or loss in accordance with the existing requirements in IAS 19; and

(b) changes in the effect of the asset ceiling are recognised in other comprehensive income as required by paragraph 57(d)(iii) of IAS 19, as a result of the reassessment of the asset ceiling based on the updated surplus, which is itself determined after the recognition of the past service cost or the gain or loss on settlement.

Do you agree with that proposal? Why or why not?

Response:

Overall, we agree with and support this amendment. However, we note that BC64 of IAS 19 has not been amended by the proposed amendments. We believe that the content of BC64 of IAS 19, as currently worded, contradicts the proposed amended paragraphs 64A, 67A, 99A, 123, 125 and 126 of IAS 19 and BC11-12 of the proposed amendments. We suggest that the wording of BC64 of IAS 19 should be either removed or replaced with wording along the lines of the above paragraphs by incorporating footnote (2) to the main text of that paragraph.

Question 3 - Interaction between the asset ceiling and past service cost or a gain or loss on settlement

Other comments

Currently, IAS 19 and IFRIC 14 have specific guidance on 'asset ceiling', which reflects the situation in which the plan assets of the defined benefit pension plan exceed the defined benefit obligation (a surplus) and whether a potential asset can be recognised with any movements posted through other comprehensive income (OCI). However, IAS 19 and IFRIC 14 are not explicit on how to account for a plan settlement in such situations. In particular, paragraph 109 of IAS 19 does not discuss how the asset ceiling should be treated when a settlement takes place. This can be illustrated by the following example:

Starting situation per year-end 2014 is the following:

Plan assets	100
Defined benefit obligation (DBO)	100
	====
Funded status	0

In the case where a surplus were to arise, this would not be deemed recoverable as a return to the employer or reduction in future premiums is not explicit in the plan. A settlement of the plan is not within the control of the entity, as this would require consent of the employees. Applying the asset ceiling test, no asset would be recognised.

The following example uses the above data as a starting point and the issue is whether the settlement loss is accounted for as either: **(a)** the difference between the defined benefit obligation (DBO) and the settlement payment (including any plan assets transferred and any payments made directly by the entity in connection with the settlement); OR **(b)** the difference between the net defined benefit asset recognised and the settlement payment?

1. ***Increase in discount rate, no settlement payment to pension fund:*** In the first half of 2015, the discount rate increases. As a result the DBO decreases to 80. This results in the following situation just before settlement:

Plan assets	100
Defined benefit obligation (DBO)	80
	====
Funded status (surplus)	20
Effect of asset ceiling	(20)
	====
Net recognised asset	0

Question 3 - Interaction between the asset ceiling and past service cost or a gain or loss on settlement

(a) *Settlement loss as the difference between DBO and the settlement payment (including any plan assets transferred and any payments made directly by the entity in connection with the settlement)*
Difference between plan assets and DBO is 20. Settlement amount is 0, so loss is 20. For the entire year, this leads to a gain of 20 in OCI (remeasurement DBO, asset ceiling and reversal of asset ceiling) and a settlement loss of 20 in profit or loss.

(b) *Settlement loss as the difference between the net defined benefit asset recognised and the settlement payment*
Difference between net recognised position and settlement amount is 0. For the entire year, this leads to no entries in OCI (remeasurement DBO and asset ceiling) and no entries in profit or loss.

2. ***Increase in discount rate, settlement payment to pension fund of 10:*** In the first half of 2015, the discount rate increases. As a result the DBO decreases to 80. This results in the following situation just before settlement:

Plan assets	100
Defined benefit obligation (DBO)	80
	====
Funded status (surplus)	20
Effect of asset ceiling	(20)
	====
Net recognised asset	0

(a) *Settlement loss as the difference between DBO and the settlement payment (including any plan assets transferred and any payments made directly by the entity in connection with the settlement)*
Difference between plan assets and DBO is 20. Settlement amount is 10, so loss is 30. For the entire year this leads to a gain of 20 in OCI (remeasurement DBO, asset ceiling and reversal of asset ceiling) and a settlement loss of 30 in profit or loss.

(b) *Settlement loss as the difference between the net defined benefit asset recognised and the settlement payment*
Difference between net recognised position and settlement amount is 10. For the entire year this leads to no entries in OCI (remeasurement DBO and asset ceiling) and a loss of 10 in profit or loss.

Question 3 - Interaction between the asset ceiling and past service cost or a gain or loss on settlement

We understand the requirements of paragraph 109 of IAS 19 would result in 'reversing' the asset ceiling through OCI, which seems not to be in line with the principles of IAS 19 that prohibit recycling of such amounts. Nonetheless, this is where a literal reading of paragraph 109 would lead. We encourage the IASB to be more explicit as to the interaction between the asset ceiling and a settlement situation and, seeking further consideration of this area, we provide below the main arguments of each accounting treatment that led to diversity in practice around this issue:

Arguments we hear from proponents of view **(a)**:

- This view is in line with paragraph 109 of IAS 19. This paragraph particularly refers to the gross elements (plan assets and DBO) and does not refer to recognised amounts.
- In this view it does not make a difference whether a payment to the plan is made or whether a settlement payment is made (avoids structuring possibilities).
- All consequences of applying the asset ceiling are accounted for in OCI. In the end, no asset ceiling is applicable, because the assets are used for settling the liability. This view results in the same profit or loss and overall OCI movement as in a situation in which no asset ceiling was applied in the first place.
- It could be argued that the assets have been recovered by means of settling the liabilities. Because of the restraints of IFRIC 14, this asset was not recognised before, but, on settlement, becomes available.

Arguments we hear from proponents of view **(b)**:

- View (a) seems to facilitate recycling of amounts recognised in OCI due to the asset ceiling test, which conflicts with the basic requirements of IAS 19, which prohibit recycling of these amounts.
- It could be argued that in this case the plan assets become available for employees. As such, the DBO should have been 100 as well. However, this conflicts with how the projected unit credit method is generally applied.
- The asset ceiling is regarded as a reduction of plan assets. As such, nothing is given up, and no profit or loss entry needs to be made.
- Some believe it is counterintuitive to account for both profit or loss and OCI, where, in effect, on a net basis, nothing happens.

Question 4 - Accounting when a plan amendment, curtailment or settlement occurs
The IASB proposes amending IAS 19 to specify that: (a) when the net defined benefit liability (asset) is remeasured in accordance with paragraph 99 of IAS 19: (i) the current service cost and the net interest after the remeasurement are determined using the assumptions applied to the remeasurement; and (ii)an entity determines the net interest after the remeasurement based on the remeasured net defined benefit liability (asset). (b) the current service cost and the net interest in the current reporting period before a plan amendment, curtailment or settlement are not affected by, or included in, the past service cost or the gain or loss on settlement. Do you agree with that proposal? Why or why not?

Response:

Overall we agree and support this amendment. However, we believe that the way the specific amendments have been proposed raises further questions that need to be clarified in order to avoid future divergence in practice.

Paragraph 67A and BC14-BC15 of the proposed amendment, as they are currently written, may be interpreted to mean that the past service cost would encompass only the part of the cost which relates to services rendered in prior periods and the current service cost would encompass the additional cost of the plan only for the period after the plan amendment. In effect, the impact of the plan amendment on the part of the current period before the plan amendment takes place, will need to be captured in the form of remeasurement, because the proposed amendment can be read as excluding it from the past service cost. We encourage the Board to be more explicit as to the determination of prior period, because we believe that the current wording, in combination with the definition of past service costs in paragraph 8 of IAS 19, may lead to misunderstanding in terms of leaving out part of the costs arising as a result of a plan amendment. We suggest that the Board considers clarifying this in the proposed paragraph 99A of IAS 19 and in BC15 to the proposed amendments.

We suggest the following revisions to the proposed amendment:

> *"99A An entity shall determine the current service cost and net interest in accordance with paragraphs 67A and 123. The current service cost and net interest* *for the period before the remeasurement that is required by paragraph 99* *shall* *not* *be* ~~*excluded*~~ *affected by* ~~*from the past service cost and from the gain or loss on*~~ *that remeasurement* ~~*settlement*~~*."*

Question 4 - Accounting when a plan amendment, curtailment or settlement occurs

"BC15 .....Consequently, the IASB concluded that the current service cost in the current reporting period before a plan amendment or curtailment should not be affected by ~~included in the past service cost~~ the plan amendment or curtailment.

In addition, we consider as meaningful at this point to raise an issue which relates to the determination of the unit of account within the scope of paragraph 99 of IAS 19. In particular, when an amendment, curtailment or settlement takes place and relates only to a group of employees, this group can potentially be considered a Unit of Account separate from the remaining employees covered by the plan. We consider that clearer guidance should be provided for the accounting treatment of such cases where there is a partial amendment, curtailment or settlement in the plan and how the provisions of paragraph 99 of IAS 19 should be applied.
This can be illustrated by the following examples:

- Suppose there is a pension plan with 1,000 employees, all being entitled to pensions and post-employment health benefits. Suppose there is a curtailment for 400 employees. Do the assumptions for the remaining 600 employees also need to be updated?
- Suppose there is a pension plan with 1,000 employees, all being entitled to pensions and post-employment health benefits. Suppose the plan is amended and the health benefits are settled. Do the assumptions for the pension part also need to be updated?

Question 5 - Transition requirements
The IASB proposes that these amendments should be applied retrospectively, but proposes providing an exemption that would be similar to that granted in respect of the amendments to IAS 19 in 2011. The exemption is for adjustments of the carrying amount of assets outside the scope of IAS 19 (for example, employee benefit expenses that are included in inventories) (see paragraph 173(a) of IAS 19). Do you agree with that proposal? Why or why not?

Response:

We generally agree with the proposed retrospective application of the amendments and the exemption similar to the one granted in respect of the amendments to IAS 19 in 2011. In addition, we support including the option for entities to early adopt the amendments.

Other additional observations:

In the IFRIC meeting held in November 2014, the Interpretations Committee discussed the proposal for an Annual Improvement to IAS 19 relating to the remeasurement of the net defined benefit liability (asset) in the event of a plan amendment or curtailment. During that meeting, it was decided that the scope of the proposal should include only the situations in which an entity remeasures the net defined benefit liability (asset) as required by paragraph 99 of IAS 19 and not to specifically refer to the 'significant market fluctuations' in IAS 34 *Interim Financial Reporting*. We also note from BC18 of the proposed amendments of this ED that the Board decided not to address the accounting in IAS 19 when "significant market fluctuations", which are referred to in paragraph B9 of IAS 34, occur during the annual reporting period.

Although we have noticed that, in situations considered as "significant market fluctuations", entities tend to follow the requirements of IAS 19 and not to remeasure the net defined benefit liability (asset), we believe that the issue of the potential mismatch between IAS 19 and IAS 34 should be addressed by the Board, either in this ED or in an Annual Improvements Project.,as the determination of "significant market fluctuations" has led to divergence in practice. Specifically, it should be clarified whether remeasurements in situations of "significant market fluctuations" would be prohibited or allowed.

Ernst & Young Global Limited
Becket House
1 Lambeth Palace Road
London
SE1 7EU

Tel: +44 [0]20 7980 0000
Fax: +44 [0]20 7980 0275
ey.com

Building a better working world

INVESTOR IN PEOPLE

International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH

9 October 2015

Dear IASB members,

Invitation to comment – Exposure Draft ED/2015/7 *Effective Date of Amendments to IFRS 10 and IAS 28*

Ernst & Young Global Limited, the central coordinating entity of the global EY organisation, welcomes the opportunity to offer its views on the Exposure Draft ED/2015/7 *Effective Date of Amendments to IFRS 10 and IAS 28* (the ED) issued by the International Accounting Standards Board (the Board) in August 2015.

We support the Board's proposal to defer the effective date of *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* (Amendments to IFRS 10 and IAS 28) indefinitely. We believe the deferral will give the Board time to consider the concerns raised about that amendment and possible conflicts with IAS 28. As there is a research project on the equity method in progress, deferral will also avoid entities having to adopt successive amendments to IAS 28 in a short time. However, we strongly recommend the Board allocates appropriate resources to the research project on the equity method so that this and other practical issues that arise on the method's application can be resolved quickly.

While we support the Board's decision to defer, we also urge the Board to use such an approach in future with caution, as it may cause confusion about the process of applying a new amendment, and the disclosures required for amendments that have been issued but are not yet effective. We believe that in this instance such an approach is appropriate given that there is a research project in progress and the amendment relates to a narrow set of circumstances.

In the Appendix we include our response to the specific question asked by the ED.

Should you wish to discuss the contents of this letter with us, please contact Leo van der Tas on +44 (0)20 7951 3152.

Yours faithfully

Ernst & Young Global Limited

Appendix

The IASB proposes to defer indefinitely the effective date *of Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* until such time as it has finalised amendments, if any, that result from its research project on the equity method. Earlier application would continue to be permitted. Do you agree with this proposal? Why or why not?

We agree with the Board's proposal to defer the effective date of *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* (Amendments to IFRS 10 and IAS 28) until the research project on the equity method is finalised.

We understand that the Board does not expect early application of the amendment to increase diversity in practice. However, we expect that existing diversity will continue and may increase, particularly as some entities may early adopt the amendment, which may reduce comparability. Therefore, we strongly recommend that the Board allocate sufficient resources to progress with the equity method research project as quickly as possible.

Ernst & Young Global Limited
Becket House
1 Lambeth Palace Road
London
SE1 7EU

Tel: +44 [0]20 7980 0000
Fax: +44 [0]20 7980 0275
ey.com

International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH
United Kingdom

28 October 2015

Dear Board members,

Invitation to comment – Exposure Draft ED/2015/6 – *Clarifications to IFRS 15*

Ernst & Young Global Limited, the central coordinating entity of the global EY organisation, welcomes the opportunity to offer its views on Exposure Draft ED/2015/6 – *Clarifications to IFRS 15* (ED) from the International Accounting Standards Board (IASB or Board).

We support the IASB's objective to provide additional clarifications and examples to reduce diversity in practice when entities adopt the new revenue standard – IFRS 15 *Revenue from Contracts with Customers* (IFRS 15 or the standard). We believe the proposed amendments would address many of the concerns raised by stakeholders about identifying performance obligations, principal-versus-agent evaluation, accounting for licences of intellectual property and transition. Overall, we believe that many of the proposed amendments would enhance the operability of IFRS 15 and result in more consistent application of judgement across entities.

We continue to support the convergence of IFRS 15 with Accounting Standards Update 2014-09, *Revenue from Contracts with Customers* (largely codified in Accounting Standards Codification (ASC) 606). For areas in which the IASB and US Financial Accounting Standards Board (FASB) (collectively known as the 'Boards') have proposed different words, but do not expect different accounting outcomes to arise, we believe that the Boards should use the same language in their respective standards and in the revised and/or new illustrative examples, such as the proposed amendments related to identifying performance obligations. This is important if the intention of the Boards is to have the same meaning and the same outcome. We believe that having different wording proposed by each Board and additional clarifications proposed by the FASB, but not the IASB, could potentially cause greater diversity in practice than expected. This is because, for example, some IFRS preparers may turn to the FASB's proposed amendments for additional guidance, while others may not.

We also note that, in the Basis for Conclusions on the ED, the IASB has included the instances in which different outcomes may arise as a consequence of different decisions made by the Boards. If the Boards did not intend to have the same meaning and are comfortable that there may be different outcomes, we believe that an explicit acknowledgement of the areas in which differences may arise between IFRS 15 and ASC 606 should be carried forward into the Basis for Conclusions on IFRS 15.

Our main comments are as summarised below (with further elaboration in Appendix A to this letter).

Identifying performance obligations

We believe that many of the proposed amendments to the illustrative examples on identifying performance obligations are helpful for entities to better understand how to evaluate the notion of 'distinct in the context of a contract' and would result in more consistent answers for similar contracts with customers.

We note that the FASB has decided to propose additional amendments to ASC 606 to clarify the evaluation of promised goods or services that are distinct in the context of the contract. We believe that the FASB's proposed amendments are helpful and should be considered by the IASB for inclusion in IFRS 15. We believe these proposed amendments would improve the operability of IFRS 15 because they clarify the overall objective, thereby making it easier for preparers to understand the 'separately identifiable' principle when assessing it in the context of a good or service.

In addition, we believe that the proposed revisions to the related illustrative examples should be the same or similar for both IFRS 15 and ASC 606 to help reduce the risk that IFRS preparers and US GAAP preparers interpret and apply the standard differently.

We are also concerned that, as currently drafted, Example 10 Case B could result in unintended consequences. In particular, it is not clear whether it was the Board's intention that the notion of a 'significant integration service' in paragraph 29(a) of IFRS 15 should be broadly applied. Without further clarification of this example, an entity could conclude that any manufacturing process includes an integration service in accordance with paragraph 29(a) of IFRS 15, because manufacturing processes include overall management of activities, such as those described in the example.

Principal versus agent application guidance

We commend the decision by the IASB and FASB to propose converged amendments to the principal versus agent application guidance. We believe that having the same language in the proposed amendments would promote comparability and improve consistency in the application of judgement across entities and industries. Accordingly, we believe that any decision by the Board to include additional application guidance in IFRS 15 or use words that are different from those in ASC 606 should be very carefully considered.

In our view, the proposed amendments do not make it clear when entities would conclude that the specified good or service is the actual good or service, or the right to a good or service, in transactions in which another party provides some or all of the goods or services to a customer. We recommend that the IASB considers expanding the application guidance in the standard and further clarify the illustrative examples.

Licences of intellectual property (IP) application guidance

We support the Board's efforts to improve the operability of the application guidance for determining the nature of an entity's promise in granting a licence and in clarifying the scope and applicability of the application guidance on sales-based and usage-based royalties related to licences of intellectual property (royalty constraint application guidance).

Under the IASB's approach, entities would have to consider the licensing application guidance when the licence is the 'primary or dominant' component in the arrangement. We are concerned about how entities may assess what is 'primary or dominant'. We recommend that the IASB considers defining 'primary or dominant' within IFRS 15 and/or providing further application guidance on how entities would assess when a promised good or service is considered primary or dominant, subject to our comment on the use of the term 'predominant' for consistency with the royalty constraint application guidance.

We also believe the differences between the FASB's proposed amendments for licences of IP in the Proposed Accounting Standards Update (ASU), *Revenue from Contracts with Customers — Identifying Performance Obligations and Licensing* issued by the FASB in May 2015 (the May 2015 Proposed ASU), from the IASB's proposed amendments, may result in different accounting outcomes. We support the use of the same language in the IASB and FASB proposed amendments, if the intention is to have the same meaning and the same outcome. However, should the Boards choose to proceed with different language, we believe it needs to be clear that entities may reach different accounting outcomes. To assist entities in understanding the areas where this may arise, we believe the Boards should consider providing a separate illustrative example with the same fact pattern that illustrates how the analysis would differ under each Board's approach. We believe the changes to the licensing application guidance are important because of the pervasive effects on many transactions. Therefore, we encourage the IASB and FASB to work together to narrow the differences between IFRS 15 and ASC 606 in this aspect of the standard to the extent possible.

Some stakeholders have questioned whether the royalty constraint application guidance in paragraph B63 of IFRS 15 is intended to relate to the timing of revenue recognition (Step 5 concept) or the determination of the transaction price (Step 3 concept). We suggest that the IASB provide further clarification in IFRS 15 regarding how the requirements for measuring progress towards the partial satisfaction of a performance obligation should be considered in instances when the royalty constraint application guidance applies.

Practical expedients on transition

We agree that the proposed practical expedients on transition will be helpful and improve the operability of IFRS 15. However, we recommend that the IASB maintains convergence on definition of 'completed contract' and proposes similar amendments to those proposed by the FASB. If the IASB disagrees with the FASB's proposal, we believe that the Board needs to explicitly clarify within the standard that, after adoption of IFRS 15, the accounting treatment for contracts that are complete on transition will be in accordance with existing IFRSs, as noted during the September 2015 IASB meeting.

We believe having the TRG is helpful as it provides a public forum for joint discussions on implementation issues that may arise in the future, even if no standard setting is required. Therefore, we support the continuation of the TRG meetings in periods leading up to the effective date of IFRS 15/ ASC 606, if and when needed. Our responses to the specific questions in the ED are provided in Appendix A.

Should you wish to discuss the contents of this letter with us, please contact Leo van der Tas on +44 20 7951 3152 or Alison Spivey on +1 202 327 6379.

Yours faithfully

Ernst & Young Global Limited

cc: Financial Accounting Standards Board

Appendix A

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?

We believe that many of the proposed amendments to the illustrative examples will help entities better understand how to evaluate the notion of 'distinct in the context of a contract' and will result in more consistent answers for similar contracts with customers.

However, we believe that the FASB's proposed amendments are needed in order to maintain convergence between IFRS 15 and ASC 606. We believe that the FASB's proposed revisions would improve the operability of IFRS 15 because they clarify the overall objective, thereby making it easier for preparers to understand the 'separately identifiable' principle when assessing it in the context of a good or service. In addition, using the same language in the proposed amendments and maintaining convergence on this aspect is important because identifying performance obligations is fundamental to the model and would have a consequential impact when applying the subsequent steps in the model. Having the same wording in this respect would help to reduce the risk of different accounting outcomes that are not intended by the Boards. Therefore, we believe the IASB should adopt the proposed revisions to paragraph 606-10-25-21 in the May 2015 Proposed ASU.

Most importantly, paragraph 29(c) of IFRS 15 currently states that a factor that indicates that an entity's promise to transfer a good or service to a customer is separately identifiable is "the good or service is not highly dependent on, or highly interrelated with, other goods or services promised in the contract". While this factor indicates that there should be a high degree of interrelationship, it does not refer to interdependency. Rather, only a high degree of dependency is needed. In the FASB's May 2015 Proposed ASU, the proposed language in paragraph 606-10-25-21(c) clarifies that goods or services should depend on each other in order to be combined into a single performance obligation. This concept is not explicitly reflected in paragraph 29(c) of IFRS 15, although it is described in paragraph BC11 of the ED. By not including the notion of interdependence in the standard, we anticipate that entities may reach different accounting conclusions under IFRS and US GAAP.

For example, assume an entity provides specialised equipment and monthly maintenance services to a customer. The monthly maintenance services are required in order to ensure the continued functionality of the equipment and are capable of being distinct because they can be provided by the entity or by other entities. When evaluating if the specialised equipment and monthly maintenance services are separately identifiable under paragraph 29(c) of IFRS 15, an entity could conclude that there is only one performance obligation, because the monthly maintenance services are required for the continued functionality of the specialised equipment. This is because the customer would not have purchased the monthly maintenance services without purchasing the specialised equipment. If the entity concludes that there is a single performance obligation, the entity would have to determine a single measure of progress to recognise revenue over time. Conversely, under the FASB's proposal, the entity could determine that the delivery of the specialised equipment to the customer is not dependent on the monthly maintenance services as the entity can satisfy its promise to deliver the specialised equipment independent of its promise to deliver the monthly maintenance services because the equipment is functional when it is transferred to the customer. Therefore, the specialised equipment and monthly maintenance services would form two performance obligations. If a greater portion of the transaction price is allocated to the specialised equipment, more revenue would be recognised upfront when that performance obligation is satisfied, whereas the revenue allocated to the maintenance services would be recognised over time.

If the Boards decide to not to use consistent wording in paragraph 29 of IFRS 15 and paragraph 606-10-25-21, it would be helpful if the Boards could explain and reconcile how the different language used would still result in the same accounting outcome reached in the related illustrative examples (i.e., Examples 10-12).

Proposed amendments to the illustrative examples in IFRS 15

We also believe that, since the IASB and FASB intend for this area to remain converged, using the same or similar wording in illustrative examples would further reduce the risk that IFRS preparers and US GAAP preparers will interpret and apply the standards differently, which may have unintended consequences. One example where different words are used is the proposed revisions to Example 11 Case A. The FASB proposed adding to the fact pattern that 'software updates' were also sold separately. However, a similar amendment was not proposed to paragraph IE49 of the ED and the reason for the difference is not apparent.

We have additional comments on the examples, as described below:

- *Example 10 Case B* – We are concerned that this example could result in unintended consequences. In particular, it is not clear whether it was the Board's intention that the notion of a 'significant integration service' in paragraph 29(a) of IFRS 15 be broadly applied. Without further clarification of this example, an entity could conclude that any manufacturing process includes an integration service in accordance with paragraph 29(a) of IFRS 15. This is because manufacturing processes include overall management of activities, such as those described in this example (i.e., procuring materials, identifying and managing sub-contractors, manufacturing or assembling goods and testing those goods). That is, as proposed, the example focuses on the entity integrating activities in order to fulfil its obligation (i.e., the input side), rather than on how the integration is part of what the customer has been promised/receives (i.e., the output side). It is not clear how integration of activities described in the example is part

of the promise to the customer. In addition, it is not clear how the entity has provided "a significant service of integrating the good or service with other goods or services promised in the contract" in accordance with paragraph 29(a) of IFRS 15. Is this conclusion based on the complexity of the end-product, the specification by the customer of the supplier(s) and/or the process that must be followed, or something in the contract that gives the customer the right to define how those things are put together? We believe clarification will be needed to differentiate the example from other manufacturing processes. Furthermore, since the example illustrates the supply of several units of the same good, it is not clear whether the example is intended to illustrate integration of the units that are promised to the customer, integration of the process to provide each unit to the customer, or both.

Subject to our comments above, we believe that this proposed example's focus on illustrating the assessment of a single factor (i.e., paragraph 29(a) of IFRS 15) is helpful. However, we recommend that the Board makes an explicit reference to paragraph 29(a) of IFRS 15 to clarify that it was the consideration of that particular factor that resulted in the conclusion and not that the promised services are highly dependent on, or highly interrelated with, each other (i.e., paragraph 29(c) of IFRS 15). The emphasis on the entity's responsibility over the management of the contract also helps bring more context to the promised services that the entity is providing to the customer, in particular, since the design services are not part of the contract. We suggest that the example be more explicit in scoping out the design aspect of the highly complex, specialised device from the arrangement so that it is clear that the contract only relates to the production process of such devices. Subject to our comments above, we recommend the following changes to paragraphs IE48A of the ED (proposed text is underlined and deleted text is ~~struck out~~):

> "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 that is not part of the current negotiated exchange. The entity is responsible for the overall management of the contract, which requires the integration of various activities including procuring materials, identifying and managing sub-contractors~~,~~ and performing manufacturing, assembly~~,~~ and testing of the devices."

- Similar to our response in relation to the proposed amendments in Example 10 Case B, we would encourage the IASB to further expand the analysis in the following proposed examples to illustrate a clearer linkage back to the factors in paragraph 29 of IFRS 15: Example 10 Case A, Example 11 Case A and Case D and Example 12 Case A. We believe this would help entities to better understand how to assess the factors and apply the requirements in the standard. For instance, for Example 11 Case A, we suggest the following changes to paragraph IE51 of the ED to expand on the rationale of why the highly interrelated or highly dependent factor is not met for the software and services:

> "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 reaching this determination, the entity considers the promises in the context of the contract and evaluates the factors in paragraph 29 of IFRS 15. 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. The software and the services are not highly interrelated or highly interdependent because the customer's ability to use and benefit from the software is not significantly affected by any of the services. The entity can fulfil its promise to grant the initial software licence independent from its promise to subsequently grant updates. The installation services do not significantly affect the customer's ability to use and benefit from the software licence because they are not complex and can be obtained from alternative providers to the extent the customer cannot perform the installation. Furthermore, the software updates in this contract do not significantly affect the customer's ability to use and benefit from the software during the licence period. ~~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~~ Therefore, 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."

- *The FASB's May 2015 Proposed ASU, Example 10 Case C* – We suggest the IASB consider including the FASB's Example 10 Case C from the FASB's May 2015 Proposed ASU. We believe that this example provides useful analysis that is not currently included in Example 55 and will be of help to constituents. That is, the FASB's Example 10, Case C illustrates how an entity should assess whether the promised goods or services are highly interrelated, which is currently not addressed by Example 55. Therefore, it lacks the analysis currently included in the FASB's proposed example.

  If the IASB decides not to include the FASB's Example 10 Case C, we suggest revising Example 55 in IFRS 15 to include the additional analysis from the FASB's proposed amendments to clarify further why the licence and software updates are highly interrelated and, therefore, not separately identifiable. Given that the IASB has decided not to propose any amendments to the standard, we believe that there will likely be greater focus on the illustrative examples in providing entities with further guidance when applying the standard. Therefore, it would be even more important to ensure consistency between Example 55 in IFRS 15 and the FASB's additional proposed illustrative example. If the FASB's Example 10 Case C is not included, we suggest the following changes to paragraphs IE278-IE280 of IFRS 15:

  "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 and the software delivered at the beginning of the arrangement would have limited benefit over the entire three-year term. The entity does not sell the updates

separately and the customer does not have the option to purchase the licence without the updates.

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 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. The licence and the updates are, in effect, inputs to a combined item in the contract because the software licence would provide the customer with little of its intended benefit absent the updates. In addition, because the updates are not functional without the base software, the licence and the updates significantly affect each other and are highly interrelated and highly interdependent such that they fulfil a single promise to the customer despite the fact the entity can fulfil its promise to grant the initial software licence independent from its promise to subsequently grant updates. Therefore, the entity concludes that ~~the licence and the updates are highly 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)."

- *Example 11 Case E* – We note that the fact pattern in this proposed example differs from the FASB's Example 11 Case E in that the consumables are only produced and sold by the entity. We believe this difference contradicts the assessment that the consumables are 'readily available', as defined in paragraph 28 of IFRS 15. That paragraph states that "a readily available resource is a good or service that is sold separately (by the entity or another entity)..." We suggest that the IASB clarifies whether it intended for the notion of readily available to include instances where the good or services are only sold separately by the entity. We also recommend that the IASB further clarifies and clearly distinguishes the difference in rationale between this example and the conclusions reached in Example 55, as it is unclear why the consumables in this example are assessed to be distinct in the context of the contract while software updates are not in Example 55 in IFRS 15.

FASB proposed practical expedients: shipping and handling

In the May 2015 Proposed ASU, the FASB has proposed a practical election to account for shipping and handling, performed after control of the good has been transferred to the customer, as a fulfilment cost. We understand that such a practical expedient would help reduce cost and complexity for entities in certain industries. While continued alignment of the revenue standards would be beneficial, we support the IASB's decision to not propose a similar practical expedient (as explained in paragraph BC24 of the ED). In particular, we believe a similar practical expedient would be a change in practice under IFRS. Having such a practical expedient may also raise more questions as to why it is limited to shipping and handling and not to other types of goods or services that may be provided after a customer has obtained control of a good, such as, storage or custodial services.

We note that the IASB has acknowledged, in paragraphs BC22 and BC24 of the ED, that this practical expedient could potentially give rise to a difference between IFRS 15 and ASC 606. Entities applying IFRS 15 would be required to identify material shipping and handling as a promised good or service and recognise some of the promised consideration in the arrangement as revenue when the shipping and handling services are performed. Entities applying ASC 606 could elect to recognise revenue earlier, when control of the good transfers to the customer. We believe that this difference should be explicitly highlighted in the Basis for Conclusions on IFRS 15 and we would encourage the Board to carry paragraphs BC22-BC24 of the ED forward into the Basis for Conclusions on IFRS 15.

FASB proposed practical expedients: immaterial in the context of the contract

In the May 2015 Proposed ASU, the FASB has proposed a practical expedient to allow entities to ignore promised goods or services that are immaterial in the context of the contract when identifying performance obligations. We understand that such a practical expedient would help reduce cost and complexity for entities applying ASC 606. However, we support the IASB's decision not to propose a similar practical expedient (as explained in paragraph BC20 and BC21 of the ED). In particular, it would be a change in practice for IFRS preparers to disregard promises when they are immaterial at the contract level, rather than at the financial statement reporting level, although in many circumstances this may lead to the same outcome.

We note that the IASB has acknowledged, in paragraphs BC17-BC21 of the ED, that this could potentially give rise to a difference between IFRS 15 and ASC 606. We support this acknowledgement and recommend that the Board carries paragraphs BC17-BC21 of the ED forward into the Basis for Conclusions on IFRS 15.

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?

We commend the decision by the IASB and FASB to propose converged amendments to the principal-versus-agent application guidance. We believe that having the same language in the proposed amendments would promote comparability and improve consistency in the application of judgement across entities and industries. In particular, we agree that the proposed revisions to paragraph B37 are helpful and would improve the operability of the standard, although significant judgement would still be required.

We also agree that it is important to, first, determine the specified good or service that will provided to the end-customer for which an entity would determine whether it is a principal or an agent. The proposed amendments and related illustrative examples help to emphasise this point and address circumstances in which implementation questions frequently arise. We also believe clarifying that an entity can be both a principal and an agent in a single contract would be helpful.

However, we recommend that the proposed application guidance be further clarified to clearly explain when an entity should identify the specified good or service as a *right* to a good or service or the *actual* good or service that will be transferred to the customer. For example, paragraph IE238D in Example 46A identifies the office maintenance services as the specified good or service, but does not explain why it is not the right to the office maintenance services. Similarly, the application of paragraph B34A(a) is not explained in Examples 47 and 48, in which the specified goods or services are determined to be the right to the service and not the actual service that the customer wants to obtain.

In addition, when the specified good or service is determined to be a right to a service under paragraph B34A(a), it is not clear how an entity should apply paragraph B35A to determine whether it is a principal in the arrangement. Our concern is best illustrated by Example 47. The entity determines that the specified good or service is a right to fly on a specified flight, which is in the form of a ticket. The entity appears to have concluded it obtained control of a good or another asset (i.e., the ticket) under paragraph B35A(a). However, the entity could inappropriately conclude that it should report revenue on a net basis because it will not have the ability to direct the airline to provide the service to the customer under paragraph B35A(b).

We believe the application guidance in the ED could be further improved by requiring entities to identify the specified good or service as the actual good or service that will be transferred to the customer; not a right to a good or service that will be provided by another party. Therefore, we suggest amending paragraph B34A of the ED as follows (proposed text is underlined and deleted text is ~~struck out~~):

> "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."

Another solution could be for the Board to further explain how to determine when the specified good or service is a right to the good or service and not the actual good or service

that the customer wants to obtain. Further clarification to the illustrative examples would be important to explain how the application guidance applies to those fact patterns.

We also recommend acknowledging explicitly in the Basis for Conclusions on IFRS 15 that an entity needs to exercise judgement in evaluating whether the specified good or service is the provision of the good or service itself or a right to the good or service and to carry forward paragraph BC51 of the ED into the Basis for Conclusions on IFRS 15.

We believe it would be helpful to incorporate aspects of Basis for Conclusions paragraph BC35 on the ED in proposed paragraph B37A to clarify that the purpose of the indicators in paragraph B37 of the ED is to support or assist in the assessment of control and not to override the application of the control principle. We believe that applying the level of judgement needed to determine whether an entity controls a good or service before it transfers to a customer will be challenging in many cases. Unless the principal-versus-agent determination is straightforward, entities will need to apply the control indicators in order to support their conclusions.

In addition, we make the following observations on the indicators:

- *Credit risk indicator* – We understand credit risk to be the risk of an entity being exposed to risk for the amount of the receivable from the customer. Paragraph B37(d) of the ED includes the following statement: "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." We think that entities may incorrectly interpret the proposed amendments to mean that the notion of 'credit risk' in the ED would constitute more than just the risks associated with the amount of a receivable due from a customer. That is, entities may incorrectly believe that the consideration of economic risks, such as an entity's obligation to pay third parties that are involved in fulfilling the contract with the customer, is required.

  Furthermore, we note that Example 46A in the ED acknowledges that there is risk related to both the customer receivable and the requirement to pay another party that is involved in providing the services. It is not clear how much weight should be given to each of those considerations in the credit risk analysis. We also note that Examples 47 and 48 in the ED evaluate credit risk (or the absence thereof) without consideration of any other economic risks.

  We believe that it would be helpful to clarify that the credit risk indicator only relates to the amount of the receivable due from a customer when the customer has no discretion in deciding whether to pay. Therefore, we suggest the below edits to paragraph B37(d) of the ED:

  > "…the entity is exposed to credit risk for the amount receivable from the customer in exchange for the specified goods or services. 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 <u>for the amount of the receivable due to the entity</u>, this may indicate that the entity is directing the other party to provide goods or services on the entity's behalf. <u>Therefore, the entity has exposure to credit risk in respect of the amount due and receivable from the customer.</u> 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."

We suggest that the interaction between paragraphs B35 and B35A of the ED be further clarified with the following edits in paragraph B35 of the ED:

"An entity is a principal if it controls the specified good or service before that good or service is transferred to a customer (see paragraph B35A). However, an entity..."

- *Inventory risk indicator* – A further improvement to paragraph B37(b) of the ED would be to expand on how inventory risks may be evaluated when assessing this indicator. Existing US GAAP (ASC 605-45-45-6) states that "evaluation of this indicator shall include arrangements between an entity and a supplier that reduce or mitigate the entity's risk level. For example, an entity's risk may be reduced significantly or essentially eliminated if the entity has the right to return unsold products to the supplier or receives inventory price protection from the supplier". We believe the IASB should consider including similar language in paragraph B37(b) to help entities better understand how to evaluate the inventory risk indicator.
- *Fulfilment risk indicator* – Paragraph B37(a) of the ED states that "the entity is primarily responsible for fulfilling the promise to provide the specified good or service. This typically includes responsibility for the acceptability of the specified good or service." Examples 46, 47 and 48 illustrate the evaluation of who is responsible for the remediation of any customer dissatisfaction after transferring the good or service. We suggest elaborating on the concept of acceptability in the fulfilment indicator as follows (proposed text is underlined):

  "This typically includes responsibility for the acceptability of the specified good or service (e.g. remediation of customer dissatisfaction)."

  We believe this would be a helpful addition since the concept of 'acceptability' is not discussed elsewhere in the standard and may not be well understood.
- Paragraphs B37(c) and B37(e), regarding the pricing latitude and credit risk indicators, include contrasting examples of when an agent may exhibit some form of these indicators, but would still be considered an agent. The fulfilment and inventory risk indicators do not include contrasting examples. Including contrasting examples in only two of the indicators (i.e., pricing latitude and credit risk) could be read to infer that, in their assessment of whether they are a principal or an agent, entities should place less weight on these indicators than on the fulfilment and inventory risk indicators. In this regard, we observe that evaluating whether an entity has fulfilment risk is not always a binary assessment and an entity may conclude that it is an agent in a transaction even if it has some level of fulfilment risk. As such, we suggest adding contrasting examples to all the indicators so that no inference could be drawn from the presence of contrasting examples in only two of the indicators.

Proposed amendments to the illustrative examples in IFRS 15

- We believe that transactions in which a retailer only momentarily obtains title of a manufacturer's products at the point of sale (sometimes referred to as 'flash title') are common across many jurisdictions. We are concerned that diversity in practice will emerge unless the standard addresses how the control principle should be assessed for

such transactions. Therefore, we recommend adding an example to illustrate how the principal versus agent application guidance should be applied for flash title transactions. We note that the staff paper from the 22 June 2015 joint Board meeting on principal versus agent considerations included an example of a retailer that had only momentarily obtained title of a manufacturer's products at the point of sale. This example was helpful in highlighting that obtaining title is not determinative and that other factors need to be considered when determining whether an entity obtains control of a good or service prior to transferring it to the customer.

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?

Overall, we support the Board's efforts to improve the operability of the application guidance for determining the nature of an entity's promise in granting a licence and in clarifying the scope and applicability of the royalty constraint application guidance.

Licence of IP application guidance

We believe the IASB's proposed amendments provide helpful clarifications on the principles to be applied in determining whether the nature of an entity's promise to grant a licence is a right to use or a right to access. Entities applying IFRS 15 will need to use judgement to assess the significance of activities it undertakes for licences of IP, which could result in entities reaching different conclusions. We note that the FASB's proposed amendments introduce new application guidance to classify IP into symbolic or functional IP that would reduce the judgement needed to apply ASC 606 and promote more consistent application under US GAAP.

As noted in our cover letter, we support the use of the same language in the IASB and FASB proposed amendments if the intention is to have the same meaning and the same outcome.

However, should the Boards choose to proceed with different language, we note that the IASB does not believe that entities will reach significantly different conclusions for the majority of licensing arrangements. As discussed below, we believe there may be instances in which entities reach different conclusions. If the Board does not agree, we recommend that the Board clarifies how the different language between its approach and the FASB's approach would result in the same accounting outcomes under various fact patterns. This would assist entities in understanding when the accounting outcomes are expected to be different and when they would be the same. Alternatively, we would encourage the IASB to revise the proposed language to ensure it is clear that entities would reach the same conclusions. We acknowledge that the FASB's approach may be more operable and could reduce the cost of applying the new standard. However, we believe that the IASB's proposed amendments are closely aligned with the principles in the standard and, therefore, on balance, we support the IASB's proposed amendments. We also agree with the proposed deletion of paragraph B57 of IFRS 15 and believe it will help entities to focus on the requirements in paragraph B58 of IFRS 15.

We have the following suggestions to further clarify the application guidance:

- Paragraph BC85 of the ED and paragraph BC407 of IFRS 15 highlight 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". Without a definition or further explanation about the notion of 'primary or dominant' in transactions involving a licence of IP, entities may incorrectly conclude that the licence is the primary or dominant component in all licensing arrangements similar to the example in paragraph BC85 of the ED. For example, if the performance obligation consists of a right to use IP plus three-year implementation services, and the IP was provided to the customer prior to the commencement of the three-year implementation services, an entity may incorrectly conclude that all the revenue would be recognised at the point the licence is transferred to the customer, given that the licence is present in the contract with the customer. Furthermore, even if an entity does not automatically conclude that a licence is always the primary or dominant component, there could be diversity in practice on how entities define 'primary or dominant' for their contracts: (a) contractual prices of each promised good or service; (b) fair value or stand-alone selling price of each promised good or service; (c) the level of effort involved for the entity to transfer each promised good or service; or (d) the customer's expected benefit from each promised good or service. Therefore, we recommend that the IASB considers defining clearly what is primary or dominant within IFRS 15 and/or provide further application guidance on how entities would assess when a promised good or service is considered primary or dominant.

  We also note that the FASB's May 2015 Proposed ASU clarifies that entities would consider the licensing application guidance for all contracts that include a licence of IP, including all instances when a licence is part of a performance obligation consisting of two or more promised goods or services, regardless of whether the licence is a primary or dominant component of an identified performance obligation. For example, in the case where an entity provides a customer with services to implement an IT system, the system implementation services are provided by the entity together with the related software licence and the entity assesses that there is only a single performance obligation (i.e., system implementation services), which includes the software licence. An entity may

have to apply the licensing application guidance under the FASB's proposed amendments, but not under the IASB's proposed amendments, if it evaluates that the licence is not the primary or dominant component of a performance obligation. If this difference is intended by the Boards, we believe that it should be explicitly acknowledged in the Basis for Conclusion on IFRS 15.

- We believe the Board should consider providing additional application guidance, such as, whether and how entities should consider the reason(s) why the promised goods or services were bundled into a combined performance obligation with a licence of IP when determining the appropriate pattern of revenue recognition (i.e., the single measure of progress). This was discussed during the July 2015 TRG meeting (although not specifically related to licences of IP). Some TRG members thought that, if a good or service is combined with other goods or services because it is not capable of being distinct, it may indicate that the good or service does not provide value or use to the customer on its own. As such, the entity would not contemplate the transfer of that good or service when determining the pattern of revenue recognition for the combined performance obligation. Conversely, if a good or service is combined with other goods or services because it is not distinct in the context of the contract, but is capable of being distinct, the single measure of progress selected would have to consider how best to reflect the different patterns of revenue recognition for the promised goods or services that have been combined into a single performance obligation. We encourage the IASB to provide additional application guidance on this issue. Without it, there could be greater diversity in practice than anticipated.

  Regardless of whether the Board provides additional application guidance on this topic, we recommend that the Board amend Example 11 Case B, Example 55 and Example 56 Case A in the ED to illustrate how the licensing application guidance should be applied. As currently written, these examples only make references to the general requirements on satisfaction of performance obligations in paragraphs 31-38 of IFRS 15, but do not explain how an entity should evaluate the licensing application guidance in combination with these general requirements. We also suggest illustrating in these examples, how the entity should determine the pattern of performance for a performance obligation consisting of two or more promised goods or services with different patterns of performance.

We would also like to highlight that the different language in the IASB and FASB's proposed amendments to the licensing application guidance may potentially result in different accounting outcomes more often than expected by the Boards. We further illustrate why in the paragraphs below and the consequential considerations for related issues that may potentially arise:

- When assessing if an entity's activities significantly affect the IP, one of the two conditions in paragraph B59A of the ED requires an entity to evaluate whether "those activities are expected to change the form (for example, the design) or the functionality …" We believe the proposed amendments to paragraph B59A of the ED are important to improve consistency in entities' judgements about whether the contract requires, or the customer reasonably expects, that the entity will undertake activities that significantly affect the IP to which the customer has rights. However, we are concerned that this may be interpreted to mean that all activities that change the form or the functionality of the

IP, regardless of whether there is a substantive change. For example, in Example 57 involving a franchise licence, the entity undertakes 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. Assume that all these activities would substantively change the form or functionality of the IP, except for operational efficiencies. Under the IASB's proposed amendments, all the activities would need to be assessed. In contrast, the FASB's approach would only require an entity to assess all those activities that substantively change the form or functionality of the IP and would disregard those that do not (i.e., operational efficiencies). Therefore, if entities are now required to evaluate more activities than just those that cause a substantive change to the form or functionality, we believe that the combination of this aspect, together with our comments above on the 'primary or dominant component' assessment, would result in greater complexity for entities. If this is not the intention of the Board, we recommend that edits be made to paragraph B59A of the ED to provide further clarification. Emphasis on activities that only result in substantive change to the form or functionality would also better align with the language in the FASB's proposed amendments.

Furthermore, it is unclear whether entities would have to evaluate past activities in addition to ongoing or future activities. For example, an entity may have performed all activities that significantly affect their brand name in the past and there are no ongoing or future activities to be undertaken. We recommend that the IASB clarifies whether entities should consider past activities that may affect the customer's ability to obtain current or future benefit from the IP in applying paragraph B59A of the ED.

In addition, we urge the Board to consider providing some examples of IP that has significant stand-alone functionality in IFRS 15. Paragraph BC65 of the ED provides specific examples of types of IP that would generally be considered to have significant stand-alone functionality. We recommend that the Board add these specific examples to IFRS 15.

In consideration of the above comments, please refer to the paragraphs below for our suggested edits to paragraph B59A of the ED, to align to the FASB's proposed amendments and incorporate the examples included in paragraph BC65 of the ED, as follows (proposed text is underlined and deleted text is ~~struck out~~):

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

(a) those <u>past or ongoing</u> activities are expected to <u>substantively</u> 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 <u>past or ongoing</u> activities. For example, the benefit from a brand is often derived from, or dependent upon, the entity's <u>past or</u> 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 (for example, the ability to process a transaction, perform a function or task, be played or aired), a substantial portion of the benefit of that intellectual property is derived from that significant stand-alone functionality. Therefore, that intellectual property would not be significantly affected by the entity's past or ongoing activities unless those past or ongoing activities change that 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)."

We believe that these changes would make the licensing application guidance in IFRS 15 more operable and would be consistent with the FASB's proposed amendments in paragraphs 606-10-55-59, 606-10-55-62 and in paragraph BC47 of the Basis for Conclusions on the May 2015 Proposed ASU.

- Paragraph B59A of the ED refers to 'the ability of the customer to obtain benefit from the IP' whereas in the May 2015 Proposed ASU, the FASB refers to utility as 'the IP's ability to provide benefits or value'. Therefore, the FASB's proposed amendments appear to include a notion of 'value' in the assessment of whether there is significant stand-alone functionality. The IASB's proposed amendments could be interpreted as being 'benefits' that only relate to the form or functionality, without consideration of whether the IP's value may be impacted. This could result in different assessment between entities that have similar transactions. For example, under the FASB's approach, an entity may have to consider if the IP is able to provide value to a customer (such as an increased sale price of products in which the IP is integrated), whereas the IASB's proposed amendments would not require such a consideration. Furthermore, the assessment could potentially give rise to different outcomes in the case when the licence provides benefit to the customer, but where it has little stand-alone value or its value cannot be demonstrated. This difference is not noted within paragraphs BC68-BC70 of the ED. We believe that the Boards should use the same words in their respective standards if the intention is to have the same meaning and assessment of utility. If the meaning and assessment is not intended to be the same, we suggest that the Boards clarify the difference in the concepts and provide guidance on how to make the assessment under IFRS 15 versus ASC 606.
- We note that the FASB proposed amendments to paragraph 606-10-55-64 in the May 2015 Proposed ASU and included additional Examples 61A and 61B to illustrate how entities should evaluate when there are contractual restrictions on the use of the licence that affects the licence's attributes, but not the nature of an entity's promise to grant the licence. For example, situations in which this could occur include when there are limits on the use of licensed IP during certain periods of time, when terms of the contract effectively revoke the customer's rights for a period of time or when the use of the licensed IP through the different platforms/distribution channels is limited to certain periods of time.

  Since the IASB has not proposed similar amendments to IFRS 15 to address such situations, we believe this could potentially result in differences between IFRS 15 and ASC 606. Such licensing arrangements are common in certain industries (e.g., media and entertainment), therefore, we believe it is important for the IASB to provide further application guidance to address when such contractual terms affect the identification of

the licence(s) granted. We urge the Board to consider including the same examples as the FASB's proposed amendments (i.e., Example 61A and 61B in the May 2015 Proposed ASU), taking into consideration the comments noted in our comment letter to the FASB, dated 30 June 2015, on the May 2015 Proposed ASU.

If the IASB does not include amendments that are similar to those proposed by the FASB, we believe it would be beneficial to carry forward paragraphs BC81-BC82 of the ED into the Basis for Conclusions on IFRS 15 and explicitly acknowledge that this could be a potential area of difference between IFRS 15 and ASC 606.

Sales-based and usage-based royalties

We support the Board's efforts to clarify the scope and applicability of the royalty constraint application guidance. We generally believe that the proposal would help alleviate confusion over when the royalty constraint application guidance should be applied. We believe it would also clarify that a royalty stream should not be accounted for partially under the general variable consideration requirements and partially under the royalty constraint application guidance.

Paragraph B63 of IFRS 15 indicates that sales or usage-based royalties promised in exchange for a licence of IP are recognised when (or as) the later of the following events: (1) the subsequent sale or usage occurs; and (2) the performance obligation to which some or all of the sales or usage-based royalty has been allocated has been satisfied (or partially satisfied). Paragraph B63 of IFRS 15 also refers to the constraint on variable consideration requirements in paragraphs 56-59 of IFRS 15, which has led some stakeholders to question whether the royalty constraint application guidance was intended to affect the determination of the transaction price (a Step 3 concept) or the timing of revenue recognition (a Step 5 concept). As explained in paragraph BC78 of the ED, the IASB decided not to clarify how an entity should account for revenue arising from royalties in exchange for a licence that provides a right to access IP when the performance obligation is partially satisfied.

Without further clarification, we believe that there may be diversity in the interpretation and application of the royalty constraint application guidance when accounting for a licence of IP that provides a right to access (an 'over-time licence') with related sales-based or usage-based royalties. We believe that some entities may interpret paragraph B63 of IFRS 15 to mean that once the underlying sale or usage occurs, an entity would be required to defer a portion of the royalties and recognise the deferred amount over the remaining licence term using an appropriate measure of progress, when the royalties relate to an over-time licence for which the licence term is only partially complete (View A). Other entities may interpret paragraph B63 of IFRS 15 to mean that, in such circumstances, an entity would recognise the full amount of royalties when the underlying sale or usage has occurred (View B). Based on Example 61 in the ED, consider the application of View A and B as follows:

An entity licenses the use of its logo for one year to a customer. The customer will pay a royalty of 5 percent of the sales price for any merchandise sold using the entity's logo. In the first month, the customer sells CU1 million of merchandise using the entity's logo and owes the entity CU50,000 in sales-based royalties. The entity determines that using a time-based measure of progress appropriately depicts its performance under the contract.

- *View A* - The entity recognises royalty revenue of CU4,167 (CU50,000 in royalties x (1 month/12 months)). It will recognise the remaining royalty revenue of CU45,833 over the remaining eleven months of the licence term.
- *View B* –The entity recognises the entire royalty revenue of CU50,000 at the end of the first month, when the underlying sale or usage has occurred.

Therefore, we suggest that the IASB provides further clarification in IFRS 15 regarding how the requirements for measuring progress towards the partial satisfaction of a performance obligation should be considered when the royalty constraint application guidance applies.

Proposed amendments to the illustrative examples in IFRS 15

Example 54 – The proposed revisions to paragraph IE277 of the ED indicate that the promise to provide the software updates does not affect the assessment of the nature of the entity's promise to transfer the software licence as a result of applying paragraph 58(c) of IFRS 15. However, we believe this explanation may be confusing given that paragraph IE276 has already indicates that the software updates are a separate performance obligation and that the unit of account for the evaluation of an entity's promise to transfer a licence under paragraph 58 of IFRS 15 is at the level of each performance obligation. While this does not change the conclusion in the example, we recommend that the Board clarify this point to avoid confusion. Therefore, we suggest the following edits:

> "The entity assesses the nature of its promise to transfer the software licence in accordance with paragraph B58 of IFRS 15. 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 and should be separately evaluated if the software updates are satisfied at a point in time or over time in accordance with paragraphs 31-38 of IFRS 15~~ 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). 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. Consequently, the entity accounts for the licence as a performance obligation satisfied at a point in time."

Other editorial comments

We recommend the following editorial changes to the wording proposed in the ED:

- Paragraph 58 of IFRS 15 includes three criteria that must be met for revenue related to a right to access licence to be recognised over time. We recommend that the word 'promised' be added to this paragraph, as follows:

"... as a result of activities of the entity that do not transfer a promised good or service to the customer."

We believe this editorial change will improve consistency within IFRS 15.

- Paragraph B62(b) of IFRS 15 explains that entities should disregard guarantees provided to a customer that a patent to IP is valid and that it will defend that patent from unauthorised use when identifying promises in a contract. We suggest the following edit to paragraph B62(b) of IFRS 15:

  "Guarantees provided by the entity that it has a valid patent to intellectual property and that it will defend and maintain that patent from unauthorised use..."

  Without this change, we think there may be confusion as to whether the Board intended for activities to maintain a patent to be identified as a promised service in an arrangement.

- Subject to our earlier comments on 'primary or dominant' component, as a further improvement, we suggest that the Board use the term 'predominant' instead of 'primary or dominant' in paragraph BC85 of the ED and paragraph BC407 of IFRS 15 to be consistent with the terminology used in paragraph B63A of the ED on the royalty constraint application guidance.

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?

We agree that the proposed practical expedients on transition would help to improve the operability of IFRS 15.

We are aware of implementation questions from stakeholders discussed during the July 2015 TRG meeting on whether the Boards intended for the definition of completed contracts to include contracts for which revenue is not yet fully recognised at the date of transition. We believe this clarification is important because it affects the population of contracts with customers that fall within the scope of the standard on transition. We note that the IASB and FASB made different decisions during their September and August 2015 meetings. Having different transition approaches may result in operational challenges for multi-nationals that

have reporting obligations under both IFRS and US GAAP. We recommend that the IASB maintains convergence on this aspect and propose similar amendments as the FASB to clarify the definition of 'completed contract' in IFRS 15. If the IASB disagrees with the FASB's tentative decision, we believe that the Board needs to explicitly clarify within IFRS 15 that, after adoption of IFRS 15, the accounting treatment for contracts that are complete on transition, will be in accordance with existing IFRSs, as noted during the September 2015 IASB meeting.

In addition, paragraph BC111 of the ED notes that an entity is permitted to apply hindsight at the beginning of the earliest period presented in accounting for contract modifications that occurred before that date (i.e., in applying paragraph C5(c) of the ED). We recommend the Board considers allowing the use of hindsight in circumstances where there are no contract modifications as this approach would provide cost relief for entities applying the standard.

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.

We note the Board's reasons (explained in paragraphs BC87-BC104 of the ED) for not proposing clarifications to IFRS 15 in respect of collectability, contract termination and non-cash consideration. However, we believe these are important aspects of the model within IFRS 15 that will affect common transactions across entities and industries. Accordingly, to reduce diversity in practice, we recommend that the IASB maintains convergence with the FASB and adopt the same clarifications in IFRS 15, where possible.

Furthermore, we understand that under current IFRS entities may be referring to the illustrative example in IAS 18 on whether an entity is acting as a principal or agent to determine the appropriate presentation of some sales taxes and levies when it is not clear that the tax is being collected on behalf of the government. Judgement may be needed to determine whether the entity or its customer is liable for the tax or levy in some situations (for example, if the entity is able to pass on some, but not all, of such costs to its customers). To encourage consistent application under IFRS 15, we recommend the Board clarifies how the presentation of sales taxes interacts with the principal versus agent application guidance (including any amendments resulting from those proposed in this ED).