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8 October 2010

The Chairman  
Australian Accounting Standards Board  
PO Box 204  
Collins Street West VIC 8007

Dear Sir,

**Response to the AASB Exposure Draft ED 198 *Revenue from Contracts with Customers*.**

I attach our response to the International Accounting Standards Board (IASB) Exposure Draft ED/2010/6 *Revenue from Contracts with Customers* for your consideration.

In addition to the attached submission, we provide the following comments with respect to the "AASB Specific Matters for Comment" set out in ED 198:

- (a) *Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:*
- (i) *not for profit entities; and*
  - (ii) *public sector entities.*

We anticipate that the linking of revenue recognition to the customer obtaining control of a service under the requirements may result in some "up-front" fees on investment management products to be deferred (as a contract liability) and recognised over the life of the contract.

Consideration should be given to whether this treatment could result in an increase to the amount of capital which is required to be held by some investment managers under their Australian Financial Services License.

We set out an alternative proposal in our attached submission to the IASB which addresses this matter.

*(b) Whether, overall, the proposals would result in financial statements that would be useful to users.*

Overall, in our view, the proposals would not result in financial statements that would be useful to users. In particular, we believe:

1. The expensing of all acquisition costs does not reflect the economic substance of some types of contracts where it is normal to recover the upfront acquisition costs over the life of a contract; and
2. The requirement to link revenue recognition for service contracts to a customer gaining "control" of the service will not always result in an intuitive outcome, in particular for non-refundable up-front fees which may now be deferred over the life of a contract.

*(c) Whether the proposals are in the best interests of the Australian and New Zealand economies.*

In general and subject to the specific matters discussed in our attached submission to the IASB, we believe that the proposal are in the best interests of the Australian and New Zealand economies.

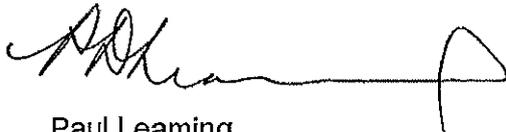
*(d) Whether any of the proposed disclosures should be considered for exclusion from the reduced disclosure requirements.*

We do not have any specific comments on this matter.

***Further discussion***

Please do not hesitate to contact Graham Duff (Manager – Accounting Policy and Advice) on 02 9257 6784 or at [graham\\_duff@amp.com.au](mailto:graham_duff@amp.com.au) if you would like to discuss any of the matters in this document.

Regards,



Paul Leaming  
Chief Financial Officer



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8 October 2010

Sir David Tweedie  
Chairman  
International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH United Kingdom

Dear Sir,

**Response to the IASB Exposure Draft ED/2010/6: *Revenue from Contracts with Customers*.**

This letter sets out the response from AMP Limited (AMP) to the International Accounting Standards Board's (IASB's) Exposure Draft ED/2010/6 *Revenue from Contracts with Customers* dated June 2010 (the ED).

AMP is generally supportive of the proposals contained in the ED in relation to the identification of separate performance obligations and the allocation of the transaction price to the separate performance obligations.

AMP does not, however, support either:

- the proposal that the recognition of revenue be recognised only on a basis that reflects the satisfaction of performance obligations to customers using a "control" criterion; or
- the proposal that an entity be required to immediately expense the cost of acquiring contracts with customers.

We provide further detail on these matters below.

The Appendix to this letter sets out our responses to the specific questions for respondents included in the ED.

AMP would like to thank the IASB for this opportunity to provide input on the changes proposed in the ED. We would appreciate any further opportunity to assist the IASB in further developing its final standard.

## **About AMP**

AMP is a leading wealth management and life insurance group operating in Australia and New Zealand with selected investment management activities in Asia and a growing banking business in Australia. AMP Limited is dual-listed on both the Australian and New Zealand stock exchanges.

## **Fulfilment of a performance obligations**

The ED proposes that revenue is not recognised until the customer obtains control of a good or service which is a performance obligation under the contract.

In our view, the timing of revenue recognition should be aligned with the work effort of the entity to fulfil the obligation under the contract with the customer. The pattern of revenue recognition which would result from adopting the requirements proposed in the ED would not reflect the work effort of the entity where an entity undertakes significant activity to fulfil its obligations under the contract in advance of the customer obtaining control of the goods or services.

Within the wealth management industry, some activities (such as setting up an account for a new customer) involve upfront costs which would not qualify as a separate performance obligation under the ED. These upfront costs may be significant and are often recovered by charging an upfront fee to the customer. Under the ED, no profit margin would be recognised on performance of these upfront activities.

In such circumstances we would propose that the completion of the work effort required to meet a performance obligation, rather than the transfer of control, provides a more relevant basis for establishing the pattern of revenue recognition which is more reflective of the economics of the transaction.

Paragraph BC30 of the basis of conclusions contends that meeting a performance obligation to a customer is the appropriate trigger for revenue recognition "because on satisfying a performance obligation, an entity no longer has the obligation to provide the good or service." In our view, this rationale would equally be applicable to completing the work effort required to meet a performance obligation.

### *AMP's proposal*

This alternative approach could be established as a requirement to recognise revenue at the earlier of:

- (a) when the customer obtains control of a good or service which is a performance obligation under the contract (as proposed in the ED); and

- (b) when all of the following conditions (based on paragraph 20 of the existing standard IAS 118 *Revenue*) are satisfied:
- (i) the entity has a contractual right to recover the revenue from the customer (although this may be subject to the future fulfilment of performance obligations);
  - (ii) the amount of revenue can be measured reliably;
  - (iii) it is probable that the economic benefits associated with the transaction will flow to the entity;
  - (iv) the stage of completion of the transaction at the end of the reporting period can be measured reliably; and
  - (v) the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

### **Contract acquisition costs**

Paragraph 59(a) of the ED requires an entity to expense the costs of obtaining a customer contract when incurred. We are concerned that this requirement is not consistent with:

- the treatment of other intangible assets which are ultimately recovered through revenue from customers;
- the treatment of acquisition costs under other current and proposed standards; and
- the principle of matching described in the IASB's *Framework for the Preparation and Presentation of Financial Statements*.

### *Inconsistency with IAS 38 Intangible Assets*

In the absence of the proposals in the ED, a valuable contract with a customer would be within the definition of an intangible asset in IAS 38 as it is an identifiable, non-monetary asset without physical substance and accordingly the costs of acquiring a contract might be eligible for capitalisation. In our view, the explicit requirement in paragraph 59(a) of the ED to expense the costs of acquiring a contract creates an inconsistency between the treatment of customer contract assets and other intangibles whose value is ultimately recovered through customer revenue.

Licensing rights, customer lists and trade marks are examples of intangible assets that are generally recovered through revenue from customer contracts. The recovery assets recognised for licensing rights, customer lists and trademarks are (all other things being equal) inherently less certain than customer contracts as for these intangible assets the entity has to first secure customer contracts and then fulfil the performance obligations.

Under the proposals in the ED, an entity would be able to recognise an asset in relation to the cost of acquiring a licensing right, customer list or trademark that was probable to generate future economic benefits through making the entity more competitive in obtaining contracts with customers. However, if an entity directly acquires customer contracts, the costs in doing so will be expensed.

#### *Inconsistency with financial instruments and insurance contracts*

Paragraph 43 of IAS 39 requires (for financial assets or liabilities not at fair value through profit or loss) that the initial measurement of the financial instrument include transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. Paragraph 39 of ED/2010/8 *Insurance Contracts* proposes that incremental acquisition costs of an insurance contract be included as part of the fulfilment cash flows of the contract. Both of these approaches result in the incremental acquisition costs being deferred and amortised over the life of the contract.

The proposal in the ED to expense all acquisition costs will therefore result in a different treatment being adopted depending on whether a particular contract is within the scope of the ED or another standard. The proposal also causes additional complexity in determining the treatment of acquisition costs for a contract which is required to be unbundled and its components accounted for separately under different standards.

#### *Matching*

Paragraph 95 of the IASB's *Framework for the Preparation and Presentation of Financial Statements* provides the following discussion on the matching principle:

*Expenses are recognised in the income statement on the basis of a direct association between the costs incurred and the earning of specific items of income. This process, commonly referred to as the matching of costs with revenues, involves the simultaneous or combined recognition of revenues and expenses that result directly and jointly from the same transactions or other events; for example, the various components of expense making up the cost of goods sold are recognised at the same time as the income derived from the sale of the goods. However, the application of the matching concept under this Framework does not allow the recognition of items in the balance sheet which do not meet the definition of assets or liabilities.*

In some cases, particularly for investment management business, up-front fees are established to recover the acquisition costs, such that from the entity's perspective, the upfront cash flows are matched. Under the ED, if the customer does not obtain control of a service at inception, the entity would be unable to recognise revenue but required to expense the costs. Thus an accounting loss would be created on an economically neutral transaction. This issue would be resolved by allowing the entity to recognise the up-front fee at inception (discussed earlier on pages 2-3).

For other contracts, a service is priced such that the up-front acquisition costs are recovered over the life of a contract. In these instances, to the extent that contract acquisition costs meet the definition of an asset, allowing the deferral of acquisition costs would appear to be more consistent with the IASB Framework than the proposed requirement that such costs be expensed as incurred.

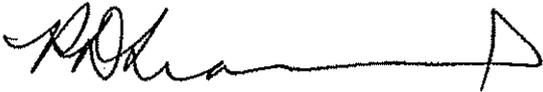
#### *AMP's proposal*

We propose that this requirement be amended to allow the deferral of incremental acquisition costs subject to a recoverability test.

***Further discussion***

Please do not hesitate to contact Graham Duff (Manager – Accounting Policy and Advice) on +61 2 9257 6784 or at [graham\\_duff@amp.com.au](mailto:graham_duff@amp.com.au) if you would like to discuss any of the matters in this document.

Regards,

A handwritten signature in black ink, appearing to read 'Paul Leaming', with a long horizontal stroke extending to the right.

Paul Leaming  
Chief Financial Officer

Cc: Mr. Kevin Stevenson, Chairman – Australian Accounting Standards Board

Appendix – detailed responses to IASB's specific request for comments

**Question 1:** Paragraphs 12–19 propose a principle (price interdependence) to help an entity determine whether:

- (a) to combine two or more contracts and account for them as a single contract;
- (b) to segment a single contract and account for it as two or more contracts; and
- (c) to account for a contract modification as a separate contract or as part of the original contract.

Do you agree with that principle? If not, what principle would you recommend, and why, for determining whether (a) to combine or segment contracts and (b) to account for a contract modification as a separate contract?

We agree with the proposal to use price interdependence as the principle to determine whether to combine or segment contracts and whether to separately account for a contract modification as a separate contract.

**Question 2:** The boards propose that an entity should identify the performance obligations to be accounted for separately on the basis of whether the promised good or service is distinct. Paragraph 23 proposes a principle for determining when a good or service is distinct. Do you agree with that principle? If not, what principle would you specify for identifying separate performance obligations and why?

We agree with the criteria proposed in paragraph 23 of the ED for determining whether a good or service is distinct.

**Question 3:** Do you think that the proposed guidance in paragraphs 25–31 and related application guidance are sufficient for determining when control of a promised good or service has been transferred to a customer? If not, why? What additional guidance would you propose and why?

The ED proposes that revenue is not recognised until the customer obtains control of a good or service which is a performance obligation under the contract.

In our view, the timing of revenue recognition should be aligned with the work effort of the entity to fulfil the obligation under the contract with the customer. The pattern of revenue recognition which would result from adopting the requirements proposed in the ED would not reflect the work effort of the entity where an entity undertakes significant activity to fulfil its obligations under the contract in advance of the customer obtaining control of the goods or services.

Within the wealth management industry, some activities (such as setting up an account for a new customer) involve upfront costs which would not qualify as a separate performance obligation under

## Appendix – detailed responses to IASB’s specific request for comments

the ED. These upfront costs may be significant and are often recovered by charging an upfront fee to the customer. Under the ED, no profit margin would be recognised on performance of these upfront activities.

In such circumstances we would propose that the completion of the work effort required to meet a performance obligation rather than the transfer of control provides a more relevant basis for establishing the pattern of revenue recognition which is more reflective of the economics of the transaction.

Paragraph BC30 of the basis of conclusions contends that meeting a performance obligation to a customer is the appropriate trigger for revenue recognition “because on satisfying a performance obligation, an entity no longer has the obligation to provide the good or service.” In our view, this rationale would equally be applicable to completing the work effort required to meet a performance obligation.

### *AMP’s proposal*

This alternative approach could be established as a requirement to recognise revenue at the earlier of:

- (a) when the customer obtains control of a good or service which is a performance obligation under the contract (as proposed in the ED); and
- (b) when all of the following conditions (based on paragraph 20 of the existing standard IAS 118 *Revenue*) are satisfied:
  - (i) the entity has a contractual right to recover the revenue from the customer (although this may be subject to the future fulfilment of performance obligations);
  - (ii) the amount of revenue can be measured reliably;
  - (iii) it is probable that the economic benefits associated with the transaction will flow to the entity;
  - (iv) the stage of completion of the transaction at the end of the reporting period can be measured reliably; and
  - (v) the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

**Question 4:** *The boards propose that if the amount of consideration is variable, an entity should recognise revenue from satisfying a performance obligation only if the transaction price can be reasonably estimated. Paragraph 38 proposes criteria that an entity should meet to be able to reasonably estimate the transaction price.*

*Do you agree that an entity should recognise revenue on the basis of an estimated transaction price? If so, do you agree with the proposed criteria in paragraph 38? If not, what approach do you suggest for recognising revenue when the transaction price is variable and why?*

## Appendix – detailed responses to IASB’s specific request for comments

We agree that an entity should recognise revenue on the basis of an estimated transaction price where that transaction price can be reasonably estimated.

We do not believe that the criteria set out paragraph 38 and 39(c) in relation to an entity's experience with similar contracts are consistent with the stated principle as an entity may be capable of preparing a reliable estimate of the transaction price without having experience with similar types of contracts, such as where the transaction price is sensitive to a single variable input and the entity has experience in reliably estimating that input, but the entity has not historically entered into contracts with variable revenue. We are also concerned that these criteria have the potential to result in inconsistent accounting treatments between market entrants and established players, as it makes the criteria revenue recognition subjective to an entity's own experience.

In our view, a better approach would be for the standard to set criteria around the level of reliability required in order for the estimate to be used and remain neutral as to the way that an entity achieves this level of reliability. We believe that the criteria set out in 39(a), (b) and (d) are useful in this regard.

**Question 5:** Paragraph 43 proposes that the transaction price should reflect the customer's credit risk if its effects on the transaction price can be reasonably estimated. Do you agree that the customer's credit risk should affect how much revenue an entity recognises when it satisfies a performance obligation rather than whether the entity recognises revenue? If not, why?

We agree with the proposal that the customer's credit risk should affect how much revenue an entity recognises rather than whether it recognises revenue. In particular, we support the approach set out in paragraph B78 of the application guidance which directs an entity to use the original invoiced amount in circumstances where the effect of the customer's credit risk on the transaction price is immaterial.

**Question 6:** Paragraphs 44 and 45 propose that an entity should adjust the amount of promised consideration to reflect the time value of money if the contract includes a material financing component (whether explicit or implicit). Do you agree? If not, why?

We agree that an entity should adjust the amount of promised consideration to reflect the time value of money if the contract includes a material financing component.

## Appendix – detailed responses to IASB’s specific request for comments

**Question 7:** Paragraph 50 proposes that an entity should allocate the transaction price to all separate performance obligations in a contract in proportion to the stand-alone selling price (estimated if necessary) of the good or service underlying each of those performance obligations. Do you agree? If not, when and why would that approach not be appropriate, and how should the transaction price be allocated in such cases?

We agree that an entity should allocate the transaction price to all separate performance obligations in proportion to the stand-alone selling price of the good or service underlying each of the performance obligations.

**Question 8:** Paragraph 57 proposes that if costs incurred in fulfilling a contract do not give rise to an asset eligible for recognition in accordance with other standards (for example, IAS 2 or ASC Topic 330; IAS 16 or ASC Topic 360; and IAS 38 Intangible Assets or ASC Topic 985 on software), an entity should recognise an asset only if those costs meet specified criteria.

Do you think that the proposed requirements on accounting for the costs of fulfilling a contract are operational and sufficient? If not, why?

Appendix C to the ED proposes that IAS 38 *Intangible Assets* be amended to exclude from its scope contract assets which are within the scope of the ED. Depending on the drafting on the amendment, this may prevent an intangible asset being recognised in relation to a customer contract even though paragraph 57 contemplates this as an example.

If the proposed amendment to IAS 38 was drafted so as to allow the recognition of separate intangible assets with respect to costs that were not recognised as part of the contract asset, then a contradiction may arise with paragraph 59(a) of the ED which requires the costs of obtaining a contract to be expensed.

We are concerned that the requirement in paragraph 59(a) to expense the costs of obtaining a contract is not consistent with:

- the treatment of other intangible assets which are ultimately recovered through revenue from customers
- the treatment of acquisition costs for financial instruments under IAS 39 and the proposed treatment of acquisition costs for insurance contracts under the IASB’s exposure draft ED/2010/8 *Insurance Contracts*
- the principle of matching described in the IASB’s *Framework for the Preparation and Presentation of Financial Statements*.

## Appendix – detailed responses to IASB's specific request for comments

### *Inconsistency with IAS 38 Intangible Assets*

A valuable contract with a customer would be within the definition of an intangible asset IAS 38 as it is an identifiable, non-monetary asset without physical substance but for the proposed changes in Appendix C of the ED explicitly removing such an asset from the scope of IAS 38. In our view, this approach creates an unnecessary inconsistency between the treatment of customer contract assets and other intangibles whose value is ultimately recovered through customer revenue.

Licensing rights, customer lists and trade marks are examples of intangible assets that are generally recovered through revenue from customer contracts. The recovery of assets recognised for licensing rights, customer lists and trademarks are (all other things being equal) inherently less certain than customer contracts as for these intangible assets the entity has to first secure customer contracts and then fulfil the performance obligations.

Under the proposals in the ED, an entity would be able to recognise an asset in relation to the cost of acquiring a licensing right, customer list or trademark that was probable to generate future economic benefits through making the entity more competitive in obtaining contracts with customers. However, if an entity directly acquires customer contracts, the costs in doing so will be expensed.

### *Inconsistency with financial instruments and insurance contracts*

Paragraph 43 of IAS 39 requires (for financial assets or liabilities not at fair value through profit or loss) that the initial measurement of the financial instrument include transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. In addition, paragraph 39 of ED/2010/8 proposes that incremental acquisition costs of an insurance contract be included as part of the fulfilment cash flows of the contract. Both of these approaches result in the incremental acquisition costs being deferred and amortised over the life of the contract.

The proposal in the ED to expense all acquisition costs will result in a different treatment being adopted depending on which standard is applicable to the contract. This will pose a particular problem in determining the treatment of acquisition costs for a contract which is required to be unbundled and its components accounted for separately under different standards.

### *Matching*

Paragraph 95 of the IASB's *Framework for the Preparation and Presentation of Financial Statements* provides the following discussion on the matching principle:

*Expenses are recognised in the income statement on the basis of a direct association between the costs incurred and the earning of specific items of income. This process, commonly referred to as the matching of costs with revenues, involves the simultaneous or combined recognition of revenues and expenses that result directly and jointly from the same transactions or other events; for example, the various components of expense making up the cost of goods sold are recognised at the same time as the income derived from the sale of the goods. However, the application of the matching concept under this Framework does not allow the recognition of items in the balance sheet which do not meet the definition of assets or liabilities.*

## Appendix – detailed responses to IASB's specific request for comments

In our view, to the extent that contract acquisition costs meet the definition of an asset, allowing the deferral of acquisition costs would be more consistent with the IASB Framework than the proposed requirement that such costs be expensed as incurred.

### *AMP's proposal*

We propose that this requirement be amended to allow the deferral of incremental acquisition costs subject to a recoverability test.

**Question 9:** Paragraph 58 proposes the costs that relate directly to a contract for the purposes of (a) recognising an asset for resources that the entity would use to satisfy performance obligations in a contract and (b) any additional liability recognised for an onerous performance obligation.

Do you agree with the costs specified? If not, what costs would you include or exclude and why?

Refer to our response to question 8 above in relation to the costs of acquiring a contract.

**Question 10:** The objective of the boards' proposed disclosure requirements is to help users of financial statements understand the amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. Do you think the proposed disclosure requirements will meet that objective? If not, why?

We believe that the proposed disclosure requirements will meet the boards' objective to help the users of financial statements understand the amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

In our view, however, the reconciliation of contract balances required by paragraph 75 appears to duplicate disclosure that would already be provided in the statement of cash flows.

### *AMP's proposal*

We propose that rather than providing a reconciliation of contract assets and contract liabilities, an entity should simply present the items required by paragraph 75(a).

**Question 11:** The boards propose that an entity should disclose the amount of its remaining performance obligations and the expected timing of their satisfaction for contracts with an original duration expected to exceed one year.

Do you agree with that proposed disclosure requirement? If not, what, if any, information do you think an entity should disclose about its remaining performance obligations?

## Appendix – detailed responses to IASB’s specific request for comments

The requirement to provide disclosure for contracts with an original duration expected to exceed one year would not provide relevant information for contracts (such as open ended service contracts) for which the entity has an expectation, but does not have an obligation to continue providing services for more than a year.

In our view, it would be more appropriate to disclose this information only for contracts where the entity is obligated to continue providing services for greater than one year.

**Question 12:** *Do you agree that an entity should disaggregate revenue into the categories that best depict how the amount, timing and uncertainty of revenue and cash flows are affected by economic factors? If not, why?*

We do not agree with the basis of disaggregation proposed in the ED. In our view it would be preferable to align any requirements to disaggregate revenue with the existing criteria for operating segment disclosure.

In our view, any required disaggregation should be aligned to operating segments disclosures where these are required under IFRS 8.

**Question 13:** *Do you agree that an entity should apply the proposed requirements retrospectively (ie as if the entity had always applied the proposed requirements to all contracts in existence during any reporting periods presented)? If not, why?*

*Is there an alternative transition method that would preserve trend information about revenue but at a lower cost? If so, please explain the alternative and why you think it is better.*

We agree that the proposed requirements should apply retrospectively.

**Question 14:** *The proposed application guidance is intended to assist an entity in applying the principles in the proposed requirements. Do you think that the application guidance is sufficient to make the proposals operational? If not, what additional guidance do you suggest?*

In our view, the application guidance is sufficient to make the proposals operational.

Appendix – detailed responses to IASB’s specific request for comments

**Question 15:** *The boards propose that an entity should distinguish between the following types of product warranties:*

*(a) a warranty that provides a customer with coverage for latent defects in the product. This does not give rise to a performance obligation but requires an evaluation of whether the entity has satisfied its performance obligation to transfer the product specified in the contract.*

*(b) a warranty that provides a customer with coverage for faults that arise after the product is transferred to the customer. This gives rise to a performance obligation in addition to the performance obligation to transfer the product specified in the contract.*

*Do you agree with the proposed distinction between the types of product warranties? Do you agree with the proposed accounting for each type of product warranty? If not, how do you think an entity should account for product warranties and why?*

We do not have any relevant comments in relation to this question.

**Question 16:** *The boards propose the following if a licence is not considered to be a sale of intellectual property:*

*(a) if an entity grants a customer an exclusive licence to use its intellectual property, it has a performance obligation to permit the use of its intellectual property and it satisfies that obligation over the term of the licence; and*

*(b) if an entity grants a customer a non-exclusive licence to use its intellectual property, it has a performance obligation to transfer the licence and it satisfies that obligation when the customer is able to use and benefit from the licence.*

*Do you agree that the pattern of revenue recognition should depend on whether the licence is exclusive? Do you agree with the patterns of revenue recognition proposed by the boards? Why or why not?*

We do not have any relevant comments in relation to this question.

Appendix – detailed responses to IASB's specific request for comments

**Question 17:** *The boards propose that in accounting for the gain or loss on the sale of some non-financial assets (for example, intangible assets and property, plant and equipment), an entity should apply the recognition and measurement principles of the proposed revenue model.*

*Do you agree? If not, why?*

We agree with the proposal that the revenue model should be applied to the sale of non-financial assets.

**Question 18 [FASB only]:** *Should any of the proposed requirements be different for non-public entities (private companies and not-for-profit organisations)? If so, which requirement(s) and why?*

Not applicable.