



Australian Government

Australian Accounting  
Standards Board

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29 April 2008

Mr Robert Garnett  
Chairman – IFRIC  
International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH  
United Kingdom

Dear Bob

**IFRIC Draft Interpretation D24**  
***Customer Contributions***

The Australian Accounting Standards Board (AASB) has considered the proposals in IFRIC Draft Interpretation D24 and is pleased to provide its views on them for consideration by the IFRIC.

The AASB has the following fundamental concerns with the proposals in D24:

- (a) It considers that the scope of the Interpretation should be narrowed and explained more clearly than in D24, or the IFRIC should not issue an Interpretation on customer contributions; and
- (b) It disagrees with the revenue recognition proposals, and considers the related Basis for Conclusions to be inadequate.

The AASB's specific comments on D24 are set out in the attached submission.

If you have any queries regarding any matters in this submission, please contact Jim Paul ([jpaul@aasb.com.au](mailto:jpaul@aasb.com.au)) or myself.

Yours sincerely

A handwritten signature in black ink that reads 'David Boymal'.

David Boymal  
Chairman

## AASB Submission on IFRIC D24 *Customer Contributions*

### Overall Comments

The AASB has the following fundamental concerns with the proposals in D24:

- (a) It considers that the scope of the Interpretation should be narrowed and explained more clearly than in D24, or the IFRIC should not issue an Interpretation on customer contributions; and
- (b) It disagrees with the revenue recognition proposals, and considers the related Basis for Conclusions to be inadequate.

These concerns are explained below.

### *Scope of the Interpretation*

The AASB observes that the scope of D24 is very broad, and D24 does not explain or provide examples to illustrate the types of arrangements it is intended to cover. Paragraph 4 says, “The customer that receives access to a supply of goods or services may contribute the asset or it may be contributed by another party.” Because there need not be a relationship between the contributor and the customer, the notion of an obligation arising from a contribution is vague and unacceptably open-ended.

### Contributions by property developers

The problem noted above is illustrated where a property developer is required to contribute infrastructure or cash to a utility company (in order to be authorised to develop an estate) without obliging the utility company to provide any access to a supply of goods or services to the developer. Sometimes, the contribution is non-refundable.

Arguably, the commitment of the utility company to provide purchasers of developed properties with ongoing access to services from the contributed asset also provides a benefit to the property developer, because that commitment enhances the value of the developed properties it sells. However, that performance obligation of the utility company does not end when the contributed assets (or assets financed by contributed cash) are fully consumed. Therefore, the AASB considers that, in this circumstance, the contribution of the asset is not the obligating event for the ongoing provision of access to future services to property holders.

The AASB considers that this example illustrates the need for the contributor to have the capacity to obtain a refund of the contributed assets or require specific performance of the promise to provide goods or services, in order for the access provider to be considered to incur a present obligation by receiving a customer contribution.

### Customer contributions to entities that are subject to a price-regulatory regime

The Australian Urgent Issues Group issued Interpretation 1017 *Developer and Customer Contributions for Connection to a Price-Regulated Network* in 1998. Its application was restricted to contributions of assets made to extend or modify a service delivery network that is subject to price regulation.

The experience in Australia has been that this Interpretation did not give rise to further issues, and that guidance has not been requested on other types of customer contributions. In view of this experience, the AASB considers that, if the Interpretation developed from D24 were restricted to the types of arrangements that gave rise to a need for guidance, it would be simpler, clearer in meaning and less likely to give rise to unintended consequences. For example, the discussion of determining whether an ongoing arrangement contains a lease could be omitted.

#### Contributions from equity participants

The broad nature of the definitions of ‘customer contribution’ and ‘cash contribution’ would appear, potentially, to include contributions from equity participants. The AASB suggests explicitly excluding contributions from equity participants, to avoid any confusion about this matter.

#### Government grants

The AASB observes that the broad definitions of ‘customer contribution’ and ‘cash contribution’ would appear to include government grants where a government is the customer. The AASB considers that it is important to acknowledge that some customer contributions within the scope of D24 would be subject to IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*, and to clarify how such grants should be treated under the Interpretation. The AASB recommends amending D24 in respect of the timing of revenue recognition for customer contributions (see below). If that amendment were supported by the IFRIC, the AASB further recommends that government grants should be excluded from the scope of the Interpretation.

#### ***Revenue Recognition***

The AASB fundamentally disagrees with the linked proposals in D24 that:

- (a) “An entity that receives an asset that meets the definition of a customer contribution has an obligation to provide access to a supply of goods or services” (paragraph 11);
- (b) “That obligation shall be reduced and revenue recognised as access to a supply of goods or services is provided” (paragraph 11); and
- (c) “The period over which revenue is recognised shall be the period over which the entity has an obligation to continue to provide access to a supply of goods or services using the contributed asset” (paragraph 16).

The AASB considers that D24’s proposed requirement for when customer contributions are recognised as revenue is a rule rather than a principle. Therefore, the requirement would not result in fundamentally different customer contribution arrangements being accounted for differently. The AASB considers that the appropriate accounting treatment of customer contributions should depend on the circumstances, such as whether:

- (a) the customer is entitled to remain connected to the network as a result of the contribution;

- (b) providing access to the network is a separate service from the sale of the products using the network; and
- (c) the contributor is entitled to discounted future goods or services as a result of making the contribution.

The AASB also considers that the Basis for Conclusions in D24 should be more robust and should include more explanation of how the proposed revenue recognition treatment reflects the requirements of IAS 18 *Revenue*. Its reasons for these comments are set out below.

The AASB considers that, depending on the terms of the arrangement, a recipient of a customer contribution may incur one or more of the following obligations (mentioned in paragraph BC17) in return for the contribution:

- (a) an obligation arising as a result of the entity agreeing to provide goods or services to the customer at a reduced price in the future;
- (b) an obligation to provide a connection to the network supplying goods and services (this may involve modifying the network to enable the customer to access the network or simply connecting the customer to the network by reading a meter and activating the customer's access to the network); and
- (c) an obligation to provide ongoing access to a supply of goods or services (generally over a specified period).

It considers that extinguishing any of these obligations gives rise to revenue.

The AASB observes that D24 proposes that the obligation in (c) will arise from all customer contributions and that extinguishing such an obligation is the only activity related to a customer contribution that gives rise to revenue of the recipient of the contribution. The AASB disagrees with both aspects of this proposal. It considers that the obligation(s) identified should depend on the terms of the arrangement involving the customer contribution. This is illustrated and explained below.

#### Customer contributions that do not give rise to an obligation for ongoing access

The AASB understands that the terms of some customer contributions oblige the recipient only to modify a service delivery network to enable the customer to access the network and then connect the customer to the network. In these cases, all of the revenue related to the customer contribution should be attributed to extinguishing those obligations, and no revenue should be deferred beyond the date of connecting the customer to the network. The AASB considers that its view is consistent with paragraph 20 of IAS 18, which requires revenue from the rendering of services to be recognised by reference to the stage of completion of the transaction at the reporting date, provided that the outcome of the transaction can be estimated reliably.

An example of customer contributions that do not give rise to an access provider's obligation to provide customers with continuing access to a supply of goods or services is an arrangement in which:

- (a) such an obligation arises instead under a separate contract or legislation;
- (b) that obligation applies equally to all of the entity's customers regardless of whether they made a contribution; and
- (c) under price regulations, the contributors must pay the same amount for future goods and services as non-contributors.

In such a case, if a customer contribution were considered to give rise to an obligation to provide customers with continuing access to a supply of goods or services, that obligation would have no economic effect because a separate contract imposes equivalent supply obligations. In other words, if customers have the same ability to access a continuing supply of goods or services, regardless of any customer contribution made to the access provider, any customer contribution they make is irrelevant to the continuing access and the access provider has no further obligation in respect of the customer contribution after providing initial access.

If the customer is not entitled to remain connected to the network as a result of the contribution, this indicates that the contribution was not made for access to an ongoing supply of goods or services.

#### Customer contributions that give rise to an obligation for ongoing access by the contributor

The AASB considers that any obligation to provide access to a supply of goods and services over a specified period should not preclude recognition of revenue for providing initial access to a network. If the cost to the entity of providing ongoing access, plus a reasonable profit margin on those costs, is small compared with the costs plus profit margin of extinguishing the entity's other obligations to the customer, it would be anomalous to recognise all of the revenue from the customer contribution as that ongoing access is provided. The AASB observes that Example 11 of the Appendix to IAS 18 provides support for this view. It says:

“When the selling price of a product includes an identifiable amount for subsequent servicing (for example, after sales support and product enhancement on the sale of software), that amount is deferred and recognised as revenue over the period during which the service is performed. *The amount deferred is that which will cover the expected costs of the services under the agreement, together with a reasonable profit on those services.*” (emphasis added)

#### Basis for Conclusions

The AASB considers that, for the following reasons, the Basis for Conclusions should provide more robust reasons for the proposals in D24 regarding the timing of revenue recognition for customer contributions.

Regarding paragraphs BC17-BC18, the AASB considers that it is illogical for the IFRIC to:

- (a) reject the view that the obligation arising from a customer contribution may relate to agreeing to provide goods or services to the customer at a reduced price in the

future because, in many cases, other customers pay the same price for those goods or services; but

- (b) support the view that the obligation arising from a customer contribution relates to providing an ongoing access to a supply of goods or services to the customer.

In the AASB's view, the fact that contributing customers sometimes pay the same price for ongoing goods or services as other customers is a reason for concluding that their contributions *do not* relate to providing an ongoing access to a supply of goods or services to the customer.

The AASB also considers that it is illogical for the IFRIC to reject the view that the obligation arising from a customer contribution may relate to providing connection to a network supplying goods and services "because, *in many cases*, once the supplier receives the asset it has a continuing obligation to use the asset to provide customers with access to a supply of goods or services" (paragraph BC18, emphasis added). This is because the IFRIC's conclusion does not address other cases.

Paragraph BC24(a) notes that one reason not to regard modifying a service delivery network to enable the customer to access the network as a service to the customer is that the customer does not obtain control of the network modification—instead, the access provider does. However, the AASB observes that the customer does obtain an asset—namely, a right of access to the network. Without the network modification, the customer would be unable to access the future supply of goods or services. Thus, by modifying the network, the access provider provides a service to the customer by remedying its existing inability to access services. Therefore, the AASB finds this reason in paragraph BC24(a) unconvincing, and considers that providing initial access to the network is a separate service from the sale of the products using the network.

The last sentence of paragraph BC24(a) notes the view that the construction or acquisition of property, plant and equipment that remains the property of the access provider should be accounted for as the construction or acquisition of an item of property, plant and equipment for use in delivering a service to the customer. Related to this, paragraph BC27 says, in brief, that construction or acquisition activity precedes the provision of benefits to the customer and therefore does not generate revenue.

The AASB observes that, in many instances, items of property, plant and equipment acquired or constructed to supply services to customers may be used to supply different customers. Thus, their benefits do not accrue to any particular customer. However, in the case of network modifications related to customer contributions, the modifications are customer-specific. Therefore, the AASB considers that revenue recognition in respect of such activities is appropriate.

## **Other Comments**

### ***Meaning of paragraph 10 of D24***

Paragraph 10 says:

"In some circumstances, the entity may be using the contributor's asset to provide access to a supply of goods or services. In such cases, the resource is not an asset of the entity."

The AASB considers that the circumstances being referred to in this quote are unclear, and observes that paragraph BC4 does not provide examples to clarify this matter. One possible reading of this quote is that it refers to the finance lease example discussed in paragraph 14. It could also apply to service concession arrangements in which an operator does not control the related property, plant and equipment but instead has an intangible asset or a financial asset. The AASB suggests that the meaning of this quote be clarified.

### ***Amortisation period***

D24 proposes that an obligation to provide access to a supply of goods or services should be reduced, and revenue recognised, over the period during which the recipient of the contributed asset has an obligation to provide access to the supply of goods or services using the contributed asset (paragraph 16). This period cannot be longer than the useful economic life of the asset (paragraph 20).

The AASB considers that, in some arrangements, the access provider's obligation to provide access to a customer would not expire at the end of the useful life of the contributed asset (or the asset acquired with a cash contribution)—for example, the extension of the service delivery network. In addition, the customer would not necessarily finance the replacement of that asset. Therefore, the AASB thinks the following comment in paragraph BC20 would not always hold true:

“... the obligation is to provide access to a supply of goods or services *using the contributed asset*”.

The AASB considers that, depending on the circumstances, the period over which a customer contribution should be amortised as revenue might exceed the useful life of the contributed asset. (For example, paragraph 18 says a law that requires a utility provider to continue to provide occupants of residential properties with access to goods or services creates an obligation to provide access. This legal requirement need not be expressed in terms of the useful life of the contributed asset.) If so, that period might be indefinite or perpetual. If it were, it would be problematic to identify when the customer contribution should be recognised as revenue.

The AASB considers that the amortisation period specified for customer contribution revenue arising from providing access to a supply of goods or services should reflect the terms of the arrangement.

### ***Accounting for a cash contribution***

Paragraph 21 says that, if the asset that must be acquired or constructed as a result of receiving a cash contribution will not meet the criteria for recognition as an item of the entity's property, plant and equipment, the entity should account for the cash contribution as proceeds for providing the asset to the customer, using IAS 11 *Construction Contracts* or IAS 18 *Revenue* as applicable.

Paragraph 22 says that if the asset that is acquired or constructed will meet the criteria for recognition as an item of the entity's property, plant and equipment, the entity has an obligation to use that asset to provide access to a supply of goods or services.

The AASB has the following concerns with these paragraphs:

- (a) it may be difficult to reliably determine in advance whether an item acquired or constructed as a result of receiving a cash contribution will meet the criteria for recognition as an asset; and
- (b) only paragraph 22 mentions that the entity will have an obligation, although the entity will have an obligation in the circumstances outlined in both paragraphs 21 and 22.

### *Time value of money*

Paragraph BC22 includes a comment that:

“The time value of money should be taken into account in measuring the revenue that is recognised.”

The AASB has the following concerns with this comment:

- (a) it is not apparent that it reflects the text of IAS 18 *Revenue*. The AASB observes that:
  - (i) paragraph 11 of IAS 18 mentions discounting future receipts of the customer’s consideration using an imputed rate of interest, but this relates to deferred inflows of the customer’s consideration. In contrast, in D24, receipt of customer contributions is not deferred; and
  - (ii) the section of IAS 18 dealing with the rendering of services requires revenue to be recognised by reference to the stage of completion of the transaction, and does not include a corresponding requirement. The following wording in paragraph 25 of IAS 18 could be regarded as contradicting the quote above from paragraph BC22 of D24:

“For practical purposes, when services are performed by an indeterminate number of acts over a specified period of time, revenue is recognised on a straight-line basis over the specified period unless there is evidence that some other method better represents the stage of completion. ...”

Furthermore, it is not apparent why the time value of money should be taken into account when recognising revenue from providing a customer with ongoing access to a network when IAS 16 *Property, Plant and Equipment* does not require it to be taken into account when recognising depreciation of the property, plant and equipment used to provide that access;

- (b) the Consensus does not mention this principle. This is inconsistent with the general policy that Bases for Conclusions should not add requirements to IFRSs;
- (c) the use of “should” rather than “shall” introduces ambiguity about whether its application is intended to be required;



- (d) the measurement of revenue in respect of a customer contribution reflects the fair value of the contributed asset(s). The time value of money affects the *allocation* of that revenue between different periods; and
- (e) no guidance is provided on precisely how the time value of money would be taken into account. For example, because the comment relates to revenue recognition rather than asset amortisation or impairment, some might interpret it as indicating that an increasing amount of revenue per period should be recognised as time passes.

In view of these concerns, the AASB suggests that the comment should be omitted. However, if it were retained, the AASB suggests that it should be included in the Consensus; that “shall” rather than “should” be used; that “allocating between periods” rather than “measuring” be used; and that guidance be provided on precisely how the time value of money would be taken into account in making that allocation.

### ***Transition***

Paragraph 24 proposes that the Interpretation be applied prospectively. Paragraph BC33 notes that historical fair values of previously contributed assets “*may not be* based on an observable price or observable inputs” (emphasis added) and therefore that it would be impracticable to apply the proposed Interpretation retrospectively. It does not provide a reason why the proposed Interpretation would not be applied retrospectively when historical fair values of previously contributed assets *are* based on an observable price or observable inputs.

### ***Drafting Comments***

#### Definitions of ‘customer contribution’ and ‘cash contribution’

Paragraph 5 defines a ‘customer contribution’ as an item of property, plant and equipment that is contributed to an access provider and a ‘cash contribution’ as a payment of cash to an access provider. However, in some places, D24 seems to use ‘customer contribution’ to refer to any type of asset contributed by a customer to an access provider (for example, see the title and paragraphs 3, 11 and 16-20).

The AASB considers that this problem could be remedied by defining ‘customer contribution’ and its components, namely, ‘cash customer contribution’ and ‘non-cash customer contribution’.

#### Meaning of ‘access provider’

The definitions of ‘customer contribution’ and ‘cash contribution’ in paragraph 5 refer to an ‘access provider’. The AASB suggests including a definition of ‘access provider’ to assist readers to understand the Interpretation.

#### Determining whether an asset has transferred

Paragraph BC4 says, “The IFRIC considered that, in *many* cases, a customer contribution will not give rise to an asset that meets the recognition criteria ...” (emphasis added). The AASB considers that it is unnecessary to say how often this circumstance will occur, and

that the quoted words imply a bias toward non-recognition of customer contributions. It recommends using the phrase “in some cases” instead.

### Editorial suggestions

The AASB has the following editorial suggestions:

- (a) Paragraph 7(b) should be amended as marked up below, because it is only addressing the measurement of contributed property, plant and equipment:

“If an entity recognises ~~an asset as a result of receiving a customer contribution~~, an item of contributed property, plant and equipment, at what amount should ~~the contributed property, plant and equipment~~ that item be initially recognised?”
- (b) The heading above paragraph BC8 should be “Recognising the contributed asset”, rather than “Recording the contributed asset”. Similarly, the first sentence of paragraph BC8 should say “initially recognised”, rather than “initially recorded”.
- (c) In the first sentence of paragraph BC9, the reference to “an ability to access a supply of goods or services” should be to “a right to access a supply of goods or services”. Corresponding amendments should be made to the second sentence of paragraph BC9 and the last two sentences of paragraph BC16.
- (d) In paragraph BC10, “recorded on initial recognition” would better be expressed as “recognised initially”.
- (e) In the last sentence of paragraph BC13, “provided sufficient guidance” should be amended to “provide sufficient guidance”.
- (f) In the last sentence of paragraph BC15, “an asset or obligation” would better be expressed as “an asset or a liability”.
- (g) In paragraph BC17(a), “goods or service” should be amended to “goods or services”.
- (h) In paragraph BC30, “was fundamentally different” should be amended to “is fundamentally different”.