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

Comments on Discussion Paper Preliminary Views on Revenue Recognition in Contracts with Customers

Thank you for the opportunity to provide comments on the Discussion Paper 'Preliminary Views on Revenue Recognition in Contracts with Customers'.

Australia and New Zealand Bank Limited (ANZ) is a bank listed on the Australian Stock Exchange. Our operations are predominantly based in Australia, New Zealand & Asia and our most recent annual results reported profits of USD2.6 billion and total assets of USD376 billion.

We support the development of a set of principles for the recognition and measurement of revenue arising from customer contracts. Although problems with revenue recognition may be more persistent in some industries than others due to variations in term, complexity and nature of customer contracts, it will serve all constituents if the existing literature on the subject can be enhanced.

In general, we agree with the underlying principle of recognising revenue on the basis of increases in an entity's net position in a contract because it is an approach that can be applied consistently to various transactions and it is consistent with the intuitive understanding that revenue is the result from an increase in assets, a decrease in liabilities or a combination of both. We do have however some observations regarding the scope of the project in relation to fees associated with financial instruments. In addition, we have some specific concerns regarding the proposal to recognise revenue only when a performance obligation has been satisfied and the proposed definition of 'control' to assess whether a performance obligation has been satisfied which are discussed in more detail below

Scope in relation to financial instruments

Based on paragraph S11 in the discussion paper we understand the Board is considering excluding financial instruments from the scope of the revenue recognition standard. We concur in general with this approach as in many cases financial

instrument related fees become part of the same unit of account as the financial instrument. For example loan origination fees become part of the effective interest rate on the originated loan, and the recognition in profit and loss of such fees should follow the measurement basis applied to the underlying financial instrument. If the underlying loan is fair valued, any fees that are an integral part of that same unit of account should be included in the fair value determination which could mean that such fees may be recognised upfront. If the loan is accounted on an amortised cost basis, the fees that are an integral part of the unit of account are recognised as yield over the expected life of the loan.

We do however note that in structuring scope exemptions for financial instrument related fees it must be considered that certain of these fee arrangements may consist of multiple performance obligations. Some may be an integral part of the financial instrument unit of account, while others embedded in the same financial instrument arrangement may contain substantive non-financial performance obligation. The intersection of fair value measurement in IAS 39 and revenue recognition is put under stress when the appropriate revenue recognition criteria for non-financial performance obligations are not met but revenue is accelerated when an item is measured at fair value. Therefore we believe it is important to define a scope exception for financial instrument fees in relation to the nature of the performance obligation (i.e., is it an integral part of the financial instrument unit of account or a separate non-financial performance obligation), rather than a blanket scope exception for financial instruments within the scope of IAS 39.

Recognise revenue only when a performance obligation is satisfied

Under the proposed model, revenue is only recognised when a performance obligation is satisfied. The discussion paper defines this as the moment when the customer obtains control of the asset (the promised good or service) which is assumed to coincide with the transfer of the asset. For long term contracts without a continuous transfer of assets (goods or services) this means that revenue is deferred until the end of the contract, while currently such contracts can qualify for the percentage of completion method (under IAS 18 paragraph 20 for services and IAS 11 paragraph 22 for construction contracts). In the proposed revenue recognition model, revenue reflects the transfer of promised goods and services to customers and not the *activities* of the entity in producing those goods and services. An entity close to satisfying a performance obligation is in a better position than an entity that has not yet started the process of fulfilling the obligation and this difference is not reflected in the proposed model. Accordingly, for certain long term contracts we do not believe that the proposed model will provide decision-useful information.

While we appreciate that deferral of revenue recognition for all contracts until a performance obligation is satisfied ensures consistency in that it eliminates the percentage of completion method, we do not believe that the Board has sufficiently considered if there are underlying differences in characteristics between contracts that currently qualify for an activities based approach (percentage of completion method) and contracts for which revenue currently is recognised upon fulfilling a performance obligation. We recommend the Board to provide a definition of revenue. The Board should specifically address the question why for long dated contracts revenue recognition as the entity progresses towards satisfying the performance obligation does not provide more decision useful information than revenue recognition just on fulfilment of the performance obligation.

Definition of control for determining when a performance obligation is satisfied

We note that the focus on control over the asset (the promised good or service) to determine whether a performance obligation has been satisfied is consistent with the use of a control test for derecognition of assets proposed in the Derecognition Exposure Draft (ED) issued in March 2009. We are however concerned by fact that the definition of control in the Discussion Paper is less comprehensive than the definition in the ED. The Discussion Paper defines obtaining control over an asset as taking physical possession, while the ED definition of control in paragraph ED IAS 39.17A acknowledges that an entity (transferor) can still have control over an asset after the entity transfers it to another entity (transferee) but the transferee does not have the practical ability to transfer the asset for the transferee's own benefit.

In other words, the ED acknowledges that an entity can still have control over an asset after the entity transfers it, but the Discussion Paper does not. We are concerned that the Discussion Paper's proposal to consider only legal ownership as the trigger for control may create an opportunity to structure contracts that allow for accelerated revenue recognition where this may not be appropriate from an economic perspective.

Should you have any queries on our comments, please contact myself at Shane.Buggle@anz.com or Rob Goss, Head of Accounting Policy, Governance and Compliance at Rob.Goss@anz.com.

Yours sincerely

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