

EUROPEAN OUTREACH ON THE IASB'S MAIN PROJECTS

EXECUTIVE SUMMARY OF THE FEEDBACK RECEIVED

JUNE 2011

Introduction

- 1 During the re-deliberations process, the IASB made some significant changes to its original proposals, in order to respond to comments received in public consultation, in relation to projects leading to the new IFRSs on revenue recognition and leases.
- 2 In order to provide European constituents with an opportunity to influence the final outcome of the projects and to eliminate whatever major concern would remain after the re-deliberations are coming to completion, EFRAG and the European national standard setters decided to organise outreach events throughout Europe in May 2011. The objective of the events was to inform European constituents of, and obtain their feedback on, the direction taken by the IASB in its re-deliberations on these two projects. The events focused only on those issues that had caused major concerns at the exposure draft stage and had been subsequently re-deliberated.
- 3 The events were held in eight European countries, including Denmark, Finland, France, Germany, Italy, the Netherlands, Spain and the United Kingdom, and were attended by a large number of constituents. Only a few users attended the meetings.
- 4 This document provides an executive summary of the feedback received during the meetings with European constituents. Additionally, EFRAG staff prepared detailed feedback statements on each event for the convenience of the European constituents. These detailed feedback statements are available on EFRAG's website and on the websites of the respective national standard setters.
- 5 The IASB and FASB have recently announced their decision to extend the convergence deadline for the projects beyond June 2011. EFRAG will meet with the IASB in June 2011 to discuss the feedback received during the outreach in Europe.

Revenue recognition

Overall feedback

- 6 In general, participants continued to question whether a complete overhaul of the existing standards on the revenue recognition was really needed, and some suggested that the direction taken by the IASB in the re-deliberations would bring the proposals quite close to the current requirements.
- 7 On a number of issues in various locations, participants did not express their views on the tentative decisions, but used the opportunity to clarify the proposals. When participants expressed their views, they generally supported the direction of the IASB's re-deliberations highlighting some areas requiring further refinements or supporting guidance. However, some constituents indicated that they would have to analyse the final standard more closely, in order to assess how it would apply to specific circumstances.

Disaggregation of contracts

- 8 When participants expressed their views, they welcomed the IASB's tentative decision that a contract, which included an "integration service", should not be disaggregated, but accounted for as a single performance obligation. However, it is worth noting that the Spanish construction Industry was not supportive of the direction of the re-deliberations, because, in their view, it went against continuous revenue recognition based on the output method.
- 9 Constituents also expressed concerns that the notion of an "integration service" may be subject to various interpretations in practice and noted a need for supporting guidance.

Timing of revenue recognition

- 10 In general, participants supported the direction of the IASB's re-deliberations on the criteria for determining if a performance obligation is satisfied continuously. However, in a number of meetings, European constituents expressed concerns that the proposals might result in revenue being recognised, even when an entity had not established a right to receive consideration subject to continued performance.
- 11 Some participants questioned whether the "alternative use of an asset" was a necessary criterion for determining whether the percentage of completion accounting could be applied. Additionally, some industries (for example, the software industry) were still concerned that, under the new proposals, they would not be able to recognise revenue continuously as work progresses (i.e., using the percentage of completion method).
- 12 In responding to the proposals in the exposure draft, telecommunication companies were concerned that the proposals would result in revenue being recognised even when payment is contingent. For example, some telecommunication companies sell a two-year subscription to a customer, providing the customer with a handset. At present, in such

situations, revenue is recognised by most – but not all – telecommunication companies as the customer is paying its monthly subscription fee. Under the proposals in the exposure draft, telecommunication companies would undoubtedly have to recognise revenue for the handset when it is delivered to the customer. Most telecommunication companies did not agree with the proposed approach, as they believed that the subscription service had to be provided in order to create a right to receive a payment from the customer. This issue has not yet been addressed by the IASB, and participants were generally anxious about it.

Uncertain consideration

- 13 Participants generally supported the direction of the IASB’s tentative decisions in relation to uncertain consideration. In particular, participants welcomed the tentative decision to limit the recognition of uncertain consideration to the amount that an entity was reasonably assured to be entitled to. Participants, in general, did not believe that revenue should be recognised when an entity was able to reasonably estimate an amount (as proposed in the exposure draft) but was not sure whether that amount would be received, for example, when a customer could avoid paying an additional amount of consideration under a sales-based royalty.

Credit risk

- 14 Overall, participants welcomed the IASB’s tentative decision not to reflect the effects of a customer’s credit risk in the measurement of the transaction price and to require presenting an allowance for any expected impairment loss from contracts with customers in a separate line on the face of the income statement.
- 15 Views on the location of the allowance within the income statement varied. Participants, in general, did not object to presenting the allowance for any expected impairment loss as contra revenue when that revenue was originally recognised. However, the majority did not support presenting subsequent remeasurement of expected losses or incurred losses next to the revenue line, as they did not relate to that revenue, and argued for the presentation of the allowance below the gross margin. However, some participants did. A few participants suggested that the standard should be flexible in respect of presentation of the allowance.

Time value of money

- 16 Overall, participants supported the direction taken by the IASB in relation to the accounting for the time value of money. However, concerns were raised about practical difficulties surrounding application of the time value of money proposals under the percentage of completion method, and it was suggested including a respective illustrative example in the final standard.

Disclosures

- 17 In those locations, where disclosures requirements were discussed, in general, there was a strong sentiment that the proposals in the exposure draft were excessive and would not result in really useful information. Participants noted that disclosure requirements should be more industry-specific and should result in information that explains the business model of the entity. Some participants noted that the proposed disclosure requirements would eliminate benefits brought by IFRS 8 *Operating Segments*.

Re-exposure of proposals

- 18 In a number of locations, participants noted that the direction taken by the IASB in the re-deliberations on the project notably deviated from the original proposals; and therefore, argued for the re-exposure of the proposals.

Leases

Overall feedback

- 19 Similar to the revenue recognition project, on a number of issues in various locations participants did not express their views on the tentative decisions, but used the opportunity to clarify the proposals or discuss application issues. However, unlike the revenue recognition project, the new proposals on leases did not receive much support, and a large number of participants believed that it would be preferable to keep IAS 17 *Leases* rather than to proceed with the new model.

Two types of leases

- 20 It is worth noting that six meetings took place in early May 2011 prior to the IASB reverting to a single model for all leases.
- 21 Overall, participants believed that not all leases were financing arrangements, and that from an economic perspective, it was sound to distinguish between two types of leases. Therefore, they appreciated that the IASB had acknowledged that fact in its re-deliberations. However, the participants seemed to perceive the dividing line between the finance and the other-than-finance leases (as discussed by the IASB prior to the May 2011 meeting) to be fairly close to the dividing line between the finance and the operating leases in the current IAS 17.
- 22 The participants, in general, argued that two different types of leases justified two different accounting treatments. However, views on the appropriate accounting treatment for leases that did not constitute primarily financing transactions were split. Some did not find the right of use model being appropriate for them, others raised concerns about the usefulness of the information produced under the modified annuity-based amortisation method (“asset-plug” model) and its complexity. The majority preferred retaining the current IAS 17 model, under which such lease arrangements are not capitalised on the balance sheet.

Definition of a lease

- 23 Overall, participants supported the direction taken by the IASB in relation to the definition of a lease; however, some participants were uncertain as to how the “specified asset” notion would be interpreted. It was indicated that the notion would be welcomed, if it were rather restrictive, and some participants believed that it was the case.

Options to extend and purchase

- 24 The IASB’s decision to include in the measurement of assets and liabilities only those amounts due under options that give a significant economic incentive to exercise, was considered an improvement compared to the exposure draft. However, participants raised

some concerns about application of the proposals and indicated that only liabilities (i.e., genuinely unavoidable payments) should be recognised in the balance sheet. Additionally, some participants noted that quite often the decision as to whether exercise an option was driven by business consideration rather than by favourable terms. An approach that would include only “non-genuine” options (similar to contingent rent) would be preferred.

Contingent rent

- 25 Overall, participants viewed the IASB’s tentative decision not to proceed with the weighted-average approach and not to include in the measurement of assets and liabilities genuine” usage-based and performance-based contingent rentals, as an improvements compared to the exposure draft. However, some participants suggested that more guidance was needed on how to identify “in substance fixed payments”. Additionally, in a number of locations, participants highlighted the importance of consistent guidance on cross-cutting issues between different standards.

Short-term leases

- 26 The IASB’s tentative decision to allow application of the simplified approach to accounting for short-term leases to both lessors and lessees, received a broad support amongst European constituents; however views on the proposed scope of the exemption of 12 months varied. Some participants suggested that 12 months was rather a short period to make the exemption really helpful, and argued for a longer period. Others suggested removing any “bright lines”. Some participants suggested that options, which did not meet the criteria of the “significant economic incentive”, should not be considered.

Re-exposure of proposals

- 27 In all locations, participants strongly argued for the re-exposure of proposals in relation to the leases project.