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Variable Consideration Cover Note

Objective

- 1 The objective of this session is for EFRAG FRB to approve the EFRAG's Discussion Paper *Accounting for Variable Consideration – From a purchaser's perspective* ('the DP') following the EFRAG FR TEG recommendation for approval made on 29 June 2022.
- 2 EFRAG FRB is also asked to recommend a suitable consultation period and provide suggestions for outreach on the DP.

Background

- 3 EFRAG FRB approved a project on Variable consideration in 2018. The project has since been under development with the extensive involvement of EFRAG FR TEG. In addition, in conducting the research, EFRAG Secretariat conducted interviews with representatives from audit firms and did a comprehensive review of past IFRS IC discussions on the topic.
- 4 EFRAG FRB received an educational session on the draft DP at its 1 June 2022 meeting. At that meeting, EFRAG FRB also expressed general support for the DP and provided comments including drafting comments that were shared via email. There was also an issue raised by a Board member on the underlying reasons for the liability recognition issue. Specifically, the assertion that IAS 32 Paragraph 25 can be interpreted differently on whether a financial liability arises for variable consideration that depends on a purchaser's future actions.
- 5 EFRAG Secretariat had a follow-up call with the Board member and thereafter had outreach calls with IASB staff and experts from the audit firms to ascertain the accuracy of the DP's analysis. Furthermore, the Board member's question was presented to the EFRAG FR TEG. The conclusion based on the outreach and EFRAG FR TEG discussion is that the DP has accurately depicted the causes of the liability recognition issue.
- 6 As noted, at its 29 June 2022 meeting, EFRAG FR TEG recommended the DP for approval to the EFRAG FRB subject to drafting changes. The main drafting change was to enhance the articulation of the reasons for different interpretations of whether the cost of an acquired asset should be updated for changes in estimates of the variable consideration. The updated drafting was subsequently shared with EFRAG FR TEG for their input to ensure it reflected all their suggested enhancements.
- 7 Apart from drafting changes to enhance the readability, coherence, and accuracy of the content in the DP, the main changes relative to the draft DP presented during the EFRAG FRB education session on 1 June 2022 are as follows:

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- (a) Executive Summary and Chapters 2 and 3, it has been made clear that the Discussion Paper is not expressing a preference for any of the alternatives for accounting requirements.
- (b) Chapter 2: The interpretation that equity classification was possible for variable consideration payments based on the interpretation of IAS 32 was deleted as there wasn't sufficient ground for this assertion.
- (c) Chapters 2 and 3: The alternatives for accounting requirements (previously referred to as approaches) have been streamlined from three to two in Chapter 2 and six to three in Chapter 3. And the Tables with advantages and disadvantages have been significantly enhanced for readability.
- (d) Chapters 2 and 3: The analysis of advantages and disadvantages no longer refers to prudence as there was an inconsistency between the application of the term as per the Conceptual Framework and the manner it was applied in the analysis.
- (e) Chapter 3: The articulation of the reasons for and against updating the cost of the acquired asset for changes in estimates of the variable consideration has been significantly enhanced including interpretations from the Conceptual Framework.
- (f) Chapters 1-3: It has been stated that it is assumed the alternatives for accounting treatment will be accompanied by disclosures. However, as disclosures are not in the scope of the project, the analysis of alternatives in Chapters 2 and 3 reflect the standalone effect on the characteristics of useful information (i.e. relevance, faithful representation, verifiability, comparability and cost-beneficial).
- (g) Chapter 4: A distinction has been made between Chapters 2 and 3 (described as Part one), which are the primary focus of the Discussion Paper and Chapter 4 (described as Part two). The objective and linkage of Chapter 4 with Chapters 2 and 3 have been further clarified.

Consultation period and outreach approach

- 8 Should EFRAG FRB approve the publication of the DP, EFRAG Secretariat recommends a targeted outreach on the DP and a consultation period until the end of June 2023. The proposed consultation period can enable possible presentations at the IFASS and ASAF and takes account of the constraints on resources.
- 9 A targeted outreach approach is appropriate as the IASB has not included a project on variable consideration in its workplan, this there is likely to be limited broad interest in the topic.

Question for EFRAG FRB

- 10 Does EFRAG FRB approve the DP for publication?
- 11 Does EFRAG FRB Board agree with a recommended consultation period until the end of June 2023?
- 12 Does EFRAG FRB have any suggestions for a targeted outreach on the DP

Agenda Papers

- 13 In addition to this cover note, agenda paper 02-02 – Draft Discussion Paper has been provided for the session.