



Accounting Standards Board

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Stig Enevoldsen
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10 April 2008

Dear Stig

Re IFRIC Draft Interpretation D24 'Customer Contributions'

The Urgent Issues Task Force (UITF) is responding on behalf of UK Accounting Standards Board (ASB) to the draft comment letter issued by EFRAG in connection with D24 'Customer Contributions'. The UITF wishes to thank EFRAG for allowing it this opportunity to comment.

The UITF has responded directly to the International Financial Reporting Interpretations Committee (IFRIC) and a copy of the letter submitted to IFRIC is attached to this paper.

The UITF is generally in agreement with the matters raised by EFRAG. As to the provisos and exceptions, noted in the draft covering letter to IFRIC, the UITF agrees with EFRAG that it would be better if explicit reference was made to IAS 18. The UITF does not however consider there is a need to rework the draft Interpretation starting from a rationale based on IAS 18.

In contrast to EFRAG, the UITF has taken the view that the scope of D24 is limited to apply only to contributions where there is an ongoing obligation to provide access. The UITF does, however, agree with EFRAG, and notes in paragraph 1 of the Appendix to its response, that the scope of the Interpretation requires clarification.

We set out in Appendix to this letter our review of EFRAG's detailed comments on IFRIC D24.

EFRAG draft comment letter - D24 Customer Contributions

Should you have any questions regarding our comments please do not hesitate to contact either Michelle Crisp or myself.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Ian Mackintosh', written in a cursive style.

Ian Mackintosh

Chairman

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Appendix to EFRAG's detailed comments on IFRIC D24

GENERAL COMMENTS

Accounting solution proposed by D24

1. The UITF does not agree with paragraph 1(b) of the draft response. The UITF does not consider that D24 requires that when an access provider receives a cash contribution it is first required to determine whether the transaction is a sale of property, plant and equipment. This is because paragraph 21 of D24 states:

"An entity that receives a cash contribution shall first consider whether the asset that must be acquired or constructed as a result of receiving the cash contribution will meet the criteria for recognition as an item property, plant and equipment of the entity. If not, the entity shall account for the cash contribution as proceeds for providing the asset to the customer, using IAS 11 or IAS 18 as applicable."

2. The UITF considers that this paragraph requires the entity to determine whether the asset to be acquired or constructed meets the definition of an asset (as in paragraph 8 of D24). Where the cash contribution does not give rise to the recognition of property, plant or equipment an entity should then consider if a sale in accordance with IAS 11 or IAS 18 has been made.

Summary of EFRAG's position

3. In paragraph 2 EFRAG states that it considers the central issue is "has there been a sale and, if there has not been a sale, what, if anything, has the access provider given up or accepted in return for the contribution". It is then noted, in paragraph 3 of the draft response, that had the issue been considered from this perspective the starting point would be IAS 18. In its response to the IFRIC the UITF noted (see paragraph 9 of the appendix to the UITF letter) that it would be helpful if specific reference was made to IAS 18. The UITF does not, however, consider that the starting point needs to be IAS 18. The UITF is of the view that the IFRIC is addressing customer contributions that are received and used to provide access to a supply of goods or services (that is future sales are made).
4. In contrast to EFRAG's view (set out in paragraph 5(a)) the UITF considers that the scope of the D24 applies only where the contribution must be used to provide access to a supply of goods or services (i.e. where there is an obligation).

DETAILED COMMENTS

Scope

5. In relation to paragraphs 6 to 10 the UITF is in agreement that the scope paragraph of the draft Interpretation could be improved. In relation to the matters raised in these paragraphs the UITF considers:
- (i) that the scope of the draft Interpretation is restricted to situations only where there is an ongoing obligation;
 - (ii) it is unclear if the draft Interpretation is limited to cases where the access must be provided with the specific item contributed;
 - (iii) D24 is applicable only to entities that receive contributions. This is because paragraph 4 (scope) states:
"The draft Interpretation applies to all situation in which an entity receives (emphasises added) an item of property, plant and equipment or cash it is ...";
 - (iv) that it should be clarified whether the draft Interpretation includes cash contributions made where the access provider transfers items of stock to property, plant and equipment.

Recognition of a customer contribution as an asset

Does the Interpretation need to say anything on this issue?

6. In its response to the IFRIC the UITF has suggested that some of the wording from this section of the draft Interpretation could be removed. However, the UITF considers that some guidance regarding whether the contributed resource qualifies for recognition as an asset is required as part of the Interpretation (see paragraphs 6 and 7 of the appendix to the UITF letter).

Definition and recognition of an asset

7. The UITF is not in agreement that paragraphs 8 to 10 of the draft Interpretation should be relabelled 'existence' and 'recognition'. In its view existence is not a term generally applied in IFRS literature. The UITF therefore considers that the current title should be retained.
8. The UITF is not in agreement with paragraph 15(a) that the material in paragraphs 9 and 10 on assessing whether the contributed resource qualifies for recognition as an asset should be expanded on and provided as application or implementation guidance.
9. In relation to paragraph 15(b) of the draft response the UITF also notes in its response to IFRIC that it is unable to locate where the material in paragraph 10 of the draft Interpretation is derived from in existing IFRS literature. The UITF

agrees IFRIC should try to avoid any confusion by using current terminology but also considers that material should be referenced to existing IFRS literature.

Measurement of the asset

10. The UITF considers measuring the asset received at fair value is appropriate. It also considers that the matters raised by EFRAG in paragraphs 16 and 17 of the draft response to IFRIC could be addressed in the drafting of the basis for conclusions to D24.

Obligation to provide access to a supply of goods of services and provision of access to a supply of goods or services

Identification of the obligation

11. The UITF is in agreement with paragraph 20 of the draft response to IFRIC and notes it raised this matter in paragraph 9 of the appendix to its response. As noted previously, in relation to paragraph 21, the UITF considers that the draft Interpretation applies only where there is an ongoing obligation.

Measurement of the obligation

12. The UITF has set out its thoughts concerning the measurement of the obligation in paragraph 8 of the appendix of its letter to IFRIC. In this paragraph the UITF notes the matter being addressed really concerns the accounting for deferred revenue as opposed to the measurement of the obligation directly and hence there is a need to reference the material in the draft Interpretation to IAS 18.

Recognition of revenue

13. In paragraph 25 EFRAG notes its concerns regarding the recognition of revenue. In its response the UITF notes that determining the period over which revenue should be recognised requires consideration of all of the contractual terms and conditions. The UITF therefore agrees with EFRAG that the period over which an entity has an obligation to provide access is subject to the facts and circumstances underlying the individual transaction.
14. The UITF considers that paragraph 26 of the draft response is unnecessary as it is clear the matter is that of accounting for deferred revenue in accordance with IAS 18.

Determining whether the ongoing arrangement contains a lease

Application of IFRIC 4

15. In paragraphs 28 to 32 it is noted that EFRAG considers that paragraph 9(a) of IFRIC 4, which provides that where the purchaser has the ability or right to operate the asset or direct others to operate the asset in a manner it determines

while obtaining or controlling more than an insignificant amount of the output or other utility of the asset, will always be achieved and that therefore there will be few assets recognised in accordance with D24. The UITF is not in agreement with this because it considers that in the situation being addressed the customer (purchaser) contributes the asset but does not have the right necessarily to operate the asset in a manner it determines. In any case the UITF considers that it is correct for an entity to determine whether the ongoing arrangement contains a lease in accordance with IFRIC 4.

Accounting for a cash contribution

16. The UITF has no comments, which it has not already raised, in relation to this section of the letter.

Transition

17. The UITF also supports prospective application.

Other comments

18. In its response to the IFRIC the UITF has suggested the terms used in D24 could be improved by referring to "customer specie contributions" and "cash contributions". The UITF has also suggested the titled of the Interpretation could be amended to clarify the scope of the Interpretation to 'Customer Contributions and Related Obligations'.



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Mr Robert Garnett
Chairman
The International Financial Reporting Interpretations
Committee of the International Accounting Standards Board
30 Cannon Street
London EC4M 6XH

12 March 2008

Dear Mr Garnett

Response to IFRIC D24 - Customer Contributions

I am writing to give the views of the Accounting Standards Board's Urgent Issues Task Force (UITF) on IFRIC D24 'Customer Contributions'.

The UITF considers that the draft Interpretation appropriately addresses an area of concern where interpretative guidance would be of use.

The UITF has considered the draft Interpretation and supports the IFRIC's decision in relation to the recognition and measurement of an asset arising from a customer contribution. The UITF, however, considers that further analysis is necessary as to measurement of the obligation arising from the contribution.

The UITF considers that the draft Interpretation implies that the credit entry arising from the contribution is deferred income rather than a liability in accordance with IAS 37 'Provisions, Contingent Liabilities and Contingent Assets'. In this regard the UITF notes that it might be helpful for the Interpretation to make specific reference to IAS 18 'Revenue' noting the inter-relationship between the two standards.

The UITF has also considered whether the fair value of the property, plant and equipment or cash that is contributed and that must be used to provide access to a supply of goods or services is evidence of the value of the performance obligation arising from the contribution. The UITF concludes that the contribution alone is not evidence and that all of the contractual terms and conditions should be assessed to determine the value of the performance obligation and how the revenue should be recognised. This matter is discussed in more detail in the appendix to this letter.

Customer contributions

The UITF also questions whether, where a cash contribution is received, the construction of the asset is never a service to the customer that generates revenue. The UITF is of the view that whether revenue is generated depends on the individual circumstances of the arrangement and the entity's normal commercial trading terms. The UITF therefore considers that an entity should be required to determine whether the construction is a revenue generating activity.

We have set out in the appendix to this letter our detailed comments regarding the draft Interpretation. Should you have any questions please do not hesitate to contact either myself or Michelle Crisp.

Yours sincerely



Ian Mackintosh
Chairman

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Appendix: UITF response to D 24 'Customer Contributions'

Scope

1. In relation to the scope of the draft Interpretation, the UITF notes it applies only in circumstances where an obligation to provide access to a supply of goods or services arises from the contributed asset. The UITF considers that the scope of the draft Interpretation could be improved, to clarify that for the Interpretation to be applicable an obligation must exist, by amending the scope paragraph as follows:

"This [draft] Interpretation applies to all situations in which an entity receives an item of property, plant and equipment or cash it is required to use to construct or acquire an item of property, plant and equipment that ~~must be used~~ it must use to provide access to a supply of goods or services. ..."

2. In making this recommendation the UITF also notes that the title of the draft Interpretation could be improved to clarify the scope of the Interpretation. The UITF suggests that the Interpretation be renamed 'Customer Contributions and Related Obligations'.
3. Also, in relation to the scope of the Interpretation, the UITF thinks that it should be made clear:
 - a. whether the draft Interpretation includes cash contributions made where the access provider transfers items of stock to property, plant and equipment; and
 - b. whether the draft Interpretation applies only where the asset contributed is used to provide access to the supply of goods or services, or whether an alternative asset may be used (i.e. the contributed asset might be grouped with other assets).

The UITF suggests that these matters are addressed as drafting issues.

Customer contributions

Definitions

4. Paragraph 5 of D24, provides a definition of a customer contribution and a cash contribution. The UITF considers that clarification of the terms could be improved by referring to contributions as – “customer specie contributions” and “cash contributions”. This would enable a distinction to be made between the two types of contributions (contributions of property, plant and equipment and cash contributions).
5. The UITF also notes that paragraph 5 uses the term “access provider”. However, there is no definition of an access provider included in the draft Interpretation.

Recognition of a customer contribution as an asset

6. The UITF is in agreement that if an entity receives a customer contribution it shall address whether the contributed resource qualifies for recognition as an asset. The UITF notes, however, that paragraph 9 states an entity shall determine whether the resource received meets the definition of an asset as well as the recognition criteria set out in the Framework. The final sentence of paragraph 9 makes reference to an assessment of the control of an asset. However, the definition of an asset includes the notion of control (a resource controlled by an entity). The UITF is not sure therefore what the final sentence of this paragraph requires an entity to do (if anything).
7. The UITF is unable to locate, in current IFRS literature, where the material that discusses control in paragraph 10 is derived from. The UITF considers that the material should be referenced to existing IFRS or IFRIC Interpretations.

Obligation to provide access to a supply of goods or services

8. As highlighted in the covering letter, the UITF is concerned that the obligation arising from the contributed asset is not always equal to the value of the asset received. The UITF notes that value of the contributed asset might be priced into the total contract and therefore the obligation to provide access to services may not always equate simply to the value of the contributed asset. However, the UITF also considers that it would be unusual to have a situation in which the measurement of a liability is not related to what has been received and therefore considers the issue being addressed in the draft Interpretation is actually about accounting for deferred revenue as opposed to measuring an obligation.

Customer contributions

9. In this regard UITF is of the view that it would be useful if IFRIC specified, in addition to the comments made in paragraph BC22, that it considers that the obligation arising is deferred revenue and that therefore IAS 18 'Revenue' is applicable, in contrast to a liability that might arise in accordance with IAS 37 'Provisions, Contingent Liabilities and Contingent Assets'.

Provision of access to a supply of goods or services

10. In relation to the period over which revenue is recognised the UITF notes the draft Interpretation does not make reference to the terms and conditions of the contract on which the entity is obliged to supply. In the UITF's view the terms and conditions of the contract need to be considered in order to determine the period over which the income should be recognised. The UITF notes that paragraph 13 of IAS 18 'Revenue' states:

"... in certain circumstances, it is necessary to apply the recognition criteria to the separately identifiable components of a single transaction in order to reflect the substance of the transaction."

11. The UITF notes it is possible for a situation to arise where an access provider may receive a contributed asset from or in respect of a customer but the terms and conditions it offers to that customer for the ongoing supply are the same terms as for all other customers. In these circumstances it is difficult to explain why an entity should defer the income to this customer. It is easier to accept deferral if the on going services are on preferential or fixed terms compared to other customers.
12. The UITF does not therefore consider that the income should always be recognised over the period which an entity has an obligation to continue to provide access to a supply of goods or services using the contributed asset.

Accounting for a cash contribution

13. As noted earlier the UITF questions whether, in the case of a cash contribution, the construction of the asset is never a service to the customer that generates revenue. The UITF is of the view that whether revenue is generated depends on the individual circumstances of the arrangement and the entity's normal commercial trading terms.
14. As noted in paragraph 8 the UITF is concerned that the value of the contributed asset or cash may not be representative of the performance obligation. In regard to a cash contribution the UITF notes, similarly, the amount of cash

Customer contributions

contributed may represent the purchase price of the asset but not necessarily represent the cost of the entity constructing the asset.

15. The UITF therefore considers that an entity should be required to determine whether the construction is a revenue generating activity by considering paragraph 13 of IAS 18.
16. The UITF notes that it might be useful in certain circumstances if the contract is “unbundled” and services considered individually.