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**IASB**

*Le Président*

**30 Cannon Street**

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**LONDON EC4M 6XH**

**N°37**

**UNITED KINGDOM**

Re: Discussion Paper "Preliminary Views on Revenue Recognition in Contracts with Customers"

Dear Madam or Sir,

I am writing on behalf of the CNC to comment on the "Preliminary Views on Revenue Recognition in Contracts with Customers" Discussion Paper (DP).

Revenue is one of the key indicators of the performance of entities. It is therefore essential to ensure that revenue recognition and measurement principles are relevant for users of financial statements, preparers, auditors and regulators.

The objective of this IASB project is to attempt to develop a single revenue recognition principle that would be applicable to all types of contracts and activities.

The CNC does not support the objective of this project. The CNC believes that a single revenue recognition principle will never be capable of reflecting the performance for all activities and, as such, would not provide decision-useful information to users. As a consequence, the CNC is also in favour of an exclusion of contracts with customers on financial instruments, insurance and leasing from this project.

In addition, as detailed hereafter, the CNC has strong reservations on the model proposed by the IASB. Consequently, the CNC considers that the IASB should not proceed with developing an ED based on the proposed model at this time.

Rather, the CNC believes that the IASB should instead launch:

- a short-term project focused on improving the existing standards by responding to difficulties already identified that are encountered in accounting for multiple-element arrangements or in distinguishing between goods and services through targeted guidance. In this regard, the CNC encourages the IASB to develop further the work already performed on these topics in the DP taking into account the feedback obtained from respondents thereon;

- a longer-term project which should start by an in-depth assessment of:
  - users' needs in terms of information on revenue;
  - how any model based on an asset and liability approach would meet those needs and how it would meet them more appropriately than the existing IFRS models;
  - what consideration should be given to the accounting treatment of costs of the contract by the entity and the accounting treatment of contracts by customers;
  - the costs and benefits of such a project for preparers compared to existing IFRSs.

In this regard, the CNC is convinced that public roundtables with constituents should be held by the IASB so as to ensure that the preliminary conclusions on this stage of the new future project on revenue recognition are shared by stakeholders before proceeding further on.

In addition, and as mentioned above, the CNC has a number of reservations about the IASB's proposed model, based on control, that go beyond a mere need of clarification:

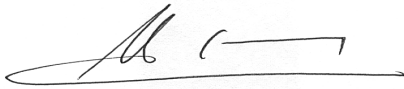
- Overall the CNC is concerned that the DP does not demonstrate how and why the proposed model based on an asset and liability approach would provide users with better quality information or that the quality of existing information provided through the application of the existing principles of IAS 18 and IAS 11 is not adequate. Please refer to our general comments in Appendix 1;
- The CNC is concerned that the DP does not consider the major impacts of this project in terms of costs for preparers and that the IASB has not conducted a robust testing of these costs in the light of the expected benefits of this project. Please refer to our general comments in Appendix 1;
- The CNC does not agree with the asset and liability model of the DP. The CNC does not share the view of the IASB that a contract gives rise, at the inception of the contract, to an asset for the rights of the entity to receive consideration from the customer and to a liability for its obligations to transfer assets to the customer. The CNC considers that the contract should only give rise to a net asset or liability that corresponds to the net position of the contract, when the contract has started to be executed by either party, with revenue generated only when the entity performs. Please refer to our answer to question 1;
- The revenue recognition model proposed, based on control, does not provide decision-useful information on the performance of the entity for some contracts for specific assets for which the execution of the contract by the entity does not coincide with the transfer of control of the asset to the customer. Please refer to our answer to question 1;
- More generally, the principle of control of an asset by the customer has not been properly worked through so that it can be applied consistently. Please refer to our answer to question 8;

- Although some progress may be achieved with the proposed model, it does not adequately respond for example to all difficulties in respect of multiple element transactions or of the distinction between goods and services. In addition, it is not clear whether it will address all the issues resolved by the existing interpretations of IFRS or submitted to the IFRIC. Consequently, the CNC considers that it does not result in any decisive improvements compared to existing standards. Please refer to our answers to questions 4 and 12 (components), 8 (distinction goods/services) and 2 (IFRIC);
- The proposed model is incomplete and as such, stakeholders are not in a position to properly assess its effects. Please refer to our general comments in Appendix 1;
- The scope of this project should be rediscussed with stakeholders to decide whether it should include a reconsideration of the accounting treatment of the costs related to a contract and as a consequence of the margin of a contract. Please refer to our general comments in Appendix 1.

Our detailed answers to the Discussion Paper's questions are set out in the Appendix 1 to this letter.

We hope you find these comments useful and would be pleased to provide any further information you might require.

Yours sincerely,



Jean-François Lepetit

## Appendix 1

### General comments (GC)

**GC.1 - Overall the CNC is concerned that the DP does not demonstrate how and why the proposed model based on an asset and liability approach would provide users with better quality information or that the quality of existing information provided through the application of the existing principles of IAS 18 and IAS 11 is not adequate**

1. The CNC agrees with the IASB on the fact that revenue is a crucial part of an entity's financial statements. It is therefore particularly important that the IASB achieves its objective of providing users with better quality information in this project, given the importance of this figure, not only for users but also for preparers, auditors and regulators.
2. The CNC notes that the IASB does not seem to have identified any major issues concerning the quality of information in its analysis of problems related to the existing revenue recognition model under IFRSs.
3. In addition, the DP does not elaborate on how the proposed model would provide better quality information. Indeed, it contains no cost-benefit analysis of the value of information that will be provided by the proposed model as compared to that of the existing model. Moreover, none of the following topics, which the CNC considers fundamental, are addressed in the DP:
  - a) What is the value of the line "revenue" for users of financial statements? Why is this figure important, relevant and decision-useful?
  - b) What level of reliability, level of certainty and confidence do users expect from revenue?
  - c) Do users share the views of the IASB that the existing model based on the co-existence of IAS 11 and IAS 18 no longer provides decision-useful information? Especially knowing that the percentage of completion method was considered useful and relevant to information needs (see IAS 11.25 that states « this method provides useful information on the extent of contract activity and performance during a period »)
  - d) If so, does the model proposed by the IASB, based on an asset and liability approach, meet their expectations?
4. The CNC believes that an in-depth analysis of the informational value of the proposed model is necessary. This analysis should not be performed globally, but should focus on the contracts and activities for which the potential effects on present practice are the most significant, for example, certain construction-type contracts, intellectual services, or activities such as software or telecommunications. This analysis should also ensure that users do not require the same information as is currently available albeit in a different form e.g. through non financial information or ratios. If this were the case, the CNC believes that this would call into question the relevance of the model proposed.

5. Such an analysis is the only way to identify what users' needs are and to validate that the model proposed in the DP meets these needs and as such the objective of better information underlying the development of an IFRS by the IASB. The CNC believes that this analysis is essential before the project is taken forward.

**GC.2 - The CNC is concerned that the DP does not consider the major impacts of this project in terms of costs for preparers and that the IASB has not conducted a robust testing of these costs in the light of the expected benefits of this project**

6. Even if the IASB says that, in developing the ED, it will consider whether the information can be provided by preparers at a reasonable cost, the CNC regrets the fact that no cost-benefit analysis has been carried out at this stage of the project. The IASB would have certainly better taken full measure of the costs that most preparers would have to bear with regard to the proposed model.
7. Indeed, the impacts of this model on information systems, internal controls, stewardship, and consistency within a group or the comparison between entities of one particular business sector are significant. For example, contracts with the same economic substance may very well be accounted for differently in the future according to their contractual terms with a group or within entities in the same business.
8. Furthermore,
  - a) information systems are currently structured around the realization of certain events that are not necessarily the same as those which will be used in the future to determine whether a performance obligation is satisfied. Preparers would be forced to make significant and costly changes to their information systems;
  - b) the identification and measurement of the various components of a contract would require establishing specific and often complex procedures. The control environment of these transactions will necessarily be heavily impacted.
9. The CNC believes that the DP represents an interesting starting point for identifying components of a contract but could result in excessive complexity and for some contracts lead to artificial unbundling. In this regard, the CNC encourages the IASB to consider the relevance of additional criteria in this process such as the stand alone value for the customer of the economic effects of contracts. However, the CNC considers that the DP does not result in any progress regarding the distinction between goods and services.

**GC.3 - The proposed model is incomplete and as such, stakeholders are not in a position to properly assess its effects**

10. The CNC fully understands the time constraints that the IASB may face. Nevertheless, the CNC believes that a project of such importance should not have resulted in the publication of a DP that deals with only a part of the revenue recognition model proposed (i.e. merely with the performance obligations).

11. Indeed, topics which are not yet discussed (refer to Appendix C of the DP) or will not at all be discussed are fundamental to correctly assess the effects of such a model. The CNC also regrets that the cross cutting issues of this project with other projects (insurance, derecognition, conceptual framework or liabilities) are not discussed nor even identified.
12. Therefore, the CNC does not believe that the stakeholders would be able to express their views on this DP in an appropriate manner.

**GC.4 - The scope of this project should be rediscussed with stakeholders to decide whether it should include a reconsideration of the accounting treatment of the costs related to a contract and as a consequence of the margin of a contract**

13. The objective of this project is to deal only with revenue recognition. Yet the CNC observes that the DP also incidentally discusses what the margin of a contract should be through the question of the subsequent assessment of certain contracts (ie "alternative" Remeasurement) or through the issue of what an onerous contract is.
14. In addition, the CNC understands that the future project is aimed at replacing both IAS 18 and IAS 11. Yet, these standards do not only address the recognition of revenue. Indeed, IAS 18 deals with the matching of costs and revenue and IAS 11 with the allocation of revenue and costs to the periods of execution of the contracts.
15. Hence the CNC does not consider it possible/reasonable to replace these two standards by a single project that deals only with revenue recognition without appropriate consideration of the treatment of costs.
16. The CNC believes that this issue is fundamental and should be debated thoroughly with stakeholders before the IASB decides how to take this project forward.

Question 1: Do you agree with the boards' proposal to base a single revenue recognition principle on changes in an entity's contract asset or contract liability? Why or why not? If not, how would you address the inconsistency in existing standards that arises from having different revenue recognition principles?

**Q1.1 - The CNC does not agree with the asset and liability model of the DP. The CNC considers that the contract should only give rise to a net asset or liability that corresponds to the net position of the contract, when the contract has started to be executed by either party, with revenue generated only when the entity performs**

17. The CNC does not share the view of the IASB that a contract gives rise, at the inception of the contract, to an asset for the rights of the entity to receive consideration from the customer and to a liability for its obligations to transfer assets to the customer.
18. On the contrary, the CNC considers that:
  - a) As far as the rights and the obligations of the entity within in a contract are equal, and neither of the parties have performed any of the promises in the contract, the entity does not have any asset or liability;

b) On the contrary when one of the parties has performed and the other has not performed proportionally, the entity should recognize an asset or a liability measured on the basis of the contract price for the net of its outstanding rights and obligations ;

c) Only the change in the net of the outstanding rights and obligations of the entity resulting from its performance within the contract gives rise to recognition of revenue (refer to the next comment for further details on the concept of performance by an entity).

19. To illustrate, for a sale of an asset to a customer:

a) it is only when the entity performs that the entity should recognise an asset for this transaction measured at the transaction price with a corresponding revenue (assuming that the customer has not paid to the entity any amount in cash relating to the contract);

b) when the customer performs (for example, by paying the totality of the price of the contract) and the entity has not yet performed, the entity should recognise a liability measured at the transaction price. No revenue should be recognised at this date as the entity has not performed any of its obligations in the contract.

**Q1.2 - The revenue recognition model proposed, based on control, does not provide decision-useful information on the performance of the entity for some contracts for specific assets for which the execution of the contract by the entity does not coincide with the transfer of control of the asset to the customer**

20. Defining a single principle of accounting for all contracts aiming at providing decision-useful information for users is conceivable only if it reflects the performance of all entities and for all activities. The CNC does not believe that such an objective is achievable given the diversity of the activities. Thus, any single principle would be simplistic and would not appropriately depict the entities' performance.

21. The proposed approach considers that, in all contracts, the entity performs only when the customer takes control of the asset (good or service) provided by the entity.

22. However, for contracts for a specific asset (such as good or a service), i.e. contracts in which the entity dedicates specific resources which can be used only for or by the customer, the CNC observes that the entity transfers these resources to this specific customer and thus performs on an ongoing basis, or, in other words as this contract is executed. In such contracts, the entity should be considered released from its obligations towards the customer when executing the contract as it is on this basis that the customer has access to the benefits of this asset, which is built specifically for him and to which no other client has any access to. Examples of such contracts may include construction type contracts (for example for a bridge or of a refinery) or service contracts.

23. These contracts are characterized by certain features such as (non-exhaustive list, indicators not necessarily cumulative):
- a) the asset is built/made to customer's specifications e.g. for example, the customer specifies the main elements of the structural elements of design of the asset before production begins and/or specifies major structural elements of the design of the asset once production is in progress;
  - b) the entity is obliged to deliver the specified asset and it is not economically feasible or practical to use other assets to fulfill this obligation;
  - c) if the customer breaches the contract, the customer is required either contractually or by the operation of law to pay a reasonable price to the entity for the costs and / or other commitments made by the entity to provide the asset.
24. Thus, for example:
- a) A customer orders a vehicle from a car manufacturer. The customer can choose various options and accessories listed in the catalog of the car manufacturer. Such a contract does not usually meet the definition of a contract for a specific asset. Indeed, the contract is a standard contract, as the customer can only exercise his choice within the limits of the offer made to him. The entity could also have produced such a vehicle regardless of an order having been placed (for its own stock). If the customer decides not to take delivery of the vehicle, the entity will probably not go to court to enforce the sale because it should be able to find another buyer without major difficulty.
  - b) A customer orders a vehicle from a car manufacturer built to his specifications with requested changes or options that are not offered in the catalog of the car manufacturer. Such a contract would normally meet the definition of a contract for a specific asset. The contract is not a standard contract. The entity would probably not have produced this vehicle if it had not received this order from this customer. The obligation of the entity is specific to this customer and to this contract. The entity cannot satisfy its obligation with another vehicle, as it is precisely this vehicle that the customer is entitled to. Moreover, if the customer decides not to take delivery of the vehicle, it is likely that the entity would obtain compensation by way of justice for the costs incurred for the production of this vehicle.
25. In such a case, as indicated above, the CNC considers that the entity should recognize an asset measured at the transaction price as the entity executes this contract together with the corresponding revenue.
26. Quite to the contrary, such revenue is not recognized in the proposed model, since the execution of the contract by the entity does not coincide with the transfer of control of the asset to the customer. Therefore, for such a contract, information on the entity's performance provided to users will be identical to information provided by an entity that performs a contract that is not specific to a customer (for example for the sale of a standard good).
27. Consequently, the CNC is of the view that the proposed model does not adequately reflect the entity's performance for all contracts. Thus, the CNC considers that the informational value of this model for users is not appropriate.



### **Q1.3 - Specific comments regarding “ the inconsistency in existing standards that arise from having different revenue recognition principles”**

28. We would like to make a specific comment about “the inconsistency in existing standards arising from having different revenue recognition principles”.
29. The CNC does not consider that having two principles for the recognition of revenue (IAS 11 and IAS 18) is the cause of the practical difficulties that may be encountered under existing IFRS for multiple-elements transactions or to distinguish goods / services.
30. The CNC is convinced that these difficulties arise from the complexity of these transactions and that having a single principle will not solve them. Moreover the CNC notes that the DP fails to resolve them completely, even if it is based on a single revenue recognition principle. The CNC considers that targeted and appropriate guidance is the only solution to address these difficulties. Please refer to our answer to questions 4 (components of a contract) and 8 (distinction goods/services).

Question 2: Are there any types of contracts for which the boards’ proposed principle would not provide decision useful information? Please provide examples and explain why. What alternative principle do you think is more useful in those examples?

#### **Q2.1 - Contracts for which the proposed principle would not provide useful information**

31. The CNC believes that the IASB’s proposed principle does not provide useful information on the entity's performance for certain contracts. Therefore, in these cases, the proposed principle does not provide decision-useful information for users. See our answer to Q1.

#### **Q2 .2 - Exclusions from the scope envisaged by the IASB on financial instruments contracts, insurance contracts and leasing contracts with customers**

32. The CNC understands that through this question, the IASB would also like to obtain the views of its stakeholders/constituents on the proposed scope exclusion for financial instruments contracts, insurance contracts or leasing contracts.
33. The objective of this IASB’s project is to attempt to develop a single revenue recognition principle that would be applicable to all types of contracts and activities.
34. The CNC does not support the objective of this project. The CNC believes that a single revenue recognition principle will never be capable of reflecting the performance for all activities and, as such, would not provide decision-useful information to users.
35. As a consequence, the CNC is also in favour of an exclusion of contracts with customers on financial instruments, insurance and leasing from this project.

36. In addition, the CNC notes that the DP does not envisage any scope exclusion for certain types of contracts which have similar characteristics to contracts with customers on financial instruments due to their volatility, for example take or pay contracts for power or a commodity , or to insurance contracts, for example product warranties. The CNC thinks it may be useful to clarify the rationale for this choice and consider whether targeted guidance is required to deal with the specific nature of these contracts.
37. Moreover, the DP seems to consider that the model may have provided useful information for some financial instruments or insurance contracts but without specifying which contracts and for what reasons. The CNC regrets the lack of information in this respect as it would have enabled stakeholders to better understand the model proposed.

### **Q2.3 - Specific issues relating to the scope of this project**

38. The CNC has identified several specific problems concerning the scope of this project. The CNC urges the IASB to make the necessary clarifications.

#### ***Future accounting treatment of certain transactions that should be excluded from the scope of the project***

39. The IASB should clarify which standards would apply in the future to certain transactions that are now in the scope of IAS 18:
- a) Revenue arising from the use by others of the entity's assets yielding interest (for example loans) for which IAS 18 refers to IAS 39;
  - b) Financial services fees on financial instruments for which we consider necessary to maintain the same level of guidance than the existing guidance in IAS 18;
  - c) Dividends (which do not arise from contracts between an entity and a customer).

#### ***Clarifications relating to royalty or licensing arrangements and more generally contracts on rights to use intangible assets***

40. The CNC requests that the IASB clarify whether this project applies to royalty, licensing arrangements or rights to use intangible assets and if so, to which ones. Indeed, the DP indicates that this project applies to contracts relating to assets, such as goods or services, but without specifying whether it also applies to rights of use of intangible assets or even of other assets.

### **Q2.4 - Necessity of a level of guidance similar to IAS 18 and to the existing interpretations**

41. The IASB should ensure that guidance equivalent to that contained in IAS 18 today and in current interpretations of IAS 18 and IAS 11 is maintained: for example on the distinction between agent and principal, or as mentioned previously on financial services fees, both topics addressed in the appendix of IAS 18 or another example on awards as addressed in IFRIC 13 (non-exhaustive list). In addition, this would allow stakeholders to gain a better understanding of the effects of the current project.

## **Q2.5 - Issues relating to revenue recognition resolved by the existing interpretations of IFRS or submitted to the IFRIC**

42. The CNC requests the IASB to ensure that:

- a) The project addresses the issues dealt with by existing IFRIC interpretations on revenue recognition (totally or partially) such as for example, IFRIC 12, IFRIC 13, IFRIC 15, IFRIC 18 or SIC 31. It should be clearly specified whether the current treatments are maintained or modified, and if so, how;
- b) The project provides appropriate answers to submissions processed or rejected by the IFRIC in recent years. These submissions reflect the concerns of stakeholders about specific issues for which the current standards do not give clear answers. The CNC considers that assessing whether the proposed model gives satisfactory answers to these issues is a robust testing of its applicability and relevance.

Question 3: Do you agree with the boards' definition of a contract? Why or why not? Please provide examples of jurisdictions or circumstances in which it would be difficult to apply that definition.

43. The CNC believes that a contract between an entity and a customer is necessary for an entity to recognize revenue.

44. In this regard, the CNC notes that the DP discusses only revenue recognition under a contract with a customer and that the IASB has not yet considered whether revenue might or not continue to be recognized in the absence of a contract between an entity and a customer (for example, under IAS 41).

### **Q3.1 - The CNC considers that the IASB's objective should be a single definition of a contract under IFRS**

45. Even if the DP states that the definition of a contract with a customer is consistent with that of IAS 32.13, the wording of these two definitions is different. The CNC is not in favor of maintaining two definitions of a contract in IFRS. The CNC believes that such a situation would only result in inconsistencies in application. Whatever decision is ultimately made by the IASB in this regard (one or two definitions), the CNC asks the IASB to examine in detail its effects and to specify them to stakeholders.

### **Q3.2 - Definition and implementation of enforceability**

46. The CNC notes that the concept of enforceability, which is essential for the definition of a contract, is not clear. A number of clarifications are necessary for a better understanding of this concept and thus, its consistent application:

- a) Should enforceable only be interpreted as “enforceable by law”? Indeed, IAS 32.13, which is considered consistent with the definition of a contract with a customer, suggests that certain contracts may not necessarily be enforceable by law as a contract is defined as “having clear economic consequences that the parties have little, if any, discretion to avoid, **usually** because the agreement is enforceable by law [**emphasis added**]”;

b) What is the relationship between the terms and conditions of a contract and its enforceability? IAS 32.13 states that a contract has "clear economic consequences." Should we thus consider that a purchase order with limited penalties in case of breach is not a contract? What does "clear economic consequence" mean? How should this concept be applied?

c) What is the role of business practice in the enforceability? in certain activities, although theoretically possible, enforceability is not implemented because the costs outweigh the benefits. Shouldn't this be taken into account?

### **Q3.3 - Firm offer versus contract**

47. The CNC considers that the DP does not discuss adequately what differentiates a firm offer from a contract to which the DP refers to .and how these two concepts are interrelated.

48. For example, the DP specifies that a firm offer is not a contract but considers at the same time that offering a discount related to a future sale as part as a contract constitutes a performance obligation to be accounted for separately.

Question 4: Do you think the boards' proposed definition of a performance obligation would help entities to identify consistently the deliverables in (or components of) a contract? Why or why not? If not, please provide examples of circumstances in which applying the proposed definition would inappropriately identify or omit deliverables in (or components of) the contract.

### **Q4.1 - General comment**

49. The CNC welcomes this proposal as a good starting point but does not consider it appropriate. The CNC observes that this proposal will result in an excessive number of components for certain contracts. The CNC considers that this approach is not sufficiently developed in order to be applicable in practice and could lead potentially to separate performance obligations that do not represent the economics of the transactions. Indeed, the provisions of DP 4.56 (rebuttable presumption, when an asset is used for another performance obligation – example of paint/painting the wall) or DP 4.60 (refer to question 5) are not sufficient for certain contracts.

50. For example, consider a subscription to the internet site of a newspaper including some special paper editions with a discount, plus a gift and a loyalty program.

51. In such a case, the CNC is not convinced that segmenting the contract on the basis of the definition of performance obligations would provide decision-useful information to the users. On the contrary, the CNC considers that this approach might result in its complexity outweighing its potential benefits.

52. Accordingly, the CNC strongly encourages the IASB to consider the relevance of additional criteria for identifying components of a contract such as:

a) the stand alone value for the customer, as for example in IFRIC 18 when assessing whether connecting the customer to a network is a separately identifiable service;

b) or the economic effects of performance obligations, as meant by IAS 27.33 which go well beyond the provisions of DP 4.56.

53. In the latter case, the CNC observes that there are interrelations between the identification of components of a contract and the combining/segmenting of contracts. In this regard, the CNC believes that the applicability to performance obligations of the guidance provided by IAS 27.33 for contracts in the case of a loss of control should be considered.
54. More generally, regarding the identification of performance obligations, the CNC faced difficulties similar to those encountered by the IASB board members, for example when analyzing the nature of a right of return or as regards the nature of certain sales incentives. Thus, the CNC fully agrees with DP § 5.23 that the process of identifying performance obligations is not without risks of errors (and not only in a context of exit value).
55. At this stage, the CNC believes that the principles proposed in the DP are not enough robust and the guidance provided is not sufficient to understand what a performance obligation really consists of. Targeted guidance is essential to result in a common understanding and application of this notion, as a basis for the identification of the components of a contract.

#### **Q4.2 - Definition of performance obligation**

56. Regarding the definition of a performance obligation, the CNC would like the IASB to clarify:
- a) What are the assets that can be transferred to a customer apart from goods and services? The use of “such as” in the definition may suggest that there may be such other assets (please refer to our answer to Q2.3 for our question on the right of use of intangible assets);
  - b) What is an implicit performance obligation? Should it be enforceable too? To what degree? Should entities also identify the constructive obligations which might arise from industry practice (i.e. the constructive obligations that others may have in the industry and on which the customer may rely)?
  - c) How to identify, recognize and measure “variable performance obligations for example, when a customer may be entitled to a variable number of products without additional payment or when new implicit obligations arise during the contract (or when any other obligation was not clearly identifiable at contract inception)? Should the segmentation be made on the basis of a more likely, probability weighted or other assessment?
  - d) How to distinguish options for a customer from firm offers?
57. In addition, the CNC observes that during the discussion on lessor accounting, the application of this single concept has led to two opposite models (sale of a right of use versus provision of a service), thus illustrating once again how difficult it is to apply this concept.

**Q4.3 – Specific comment on the statutory warranty: the statutory warranty does not meet the definition of a separate performance obligation**

58. The CNC believes that the statutory warranty – when imposed by local law or operation of law - has not been discussed and analyzed appropriately.
59. As opposed to additional warranty services (for free or not), the statutory warranty cannot be separated from the initial sale of the asset. Indeed, the entity cannot sell the asset without it in virtue of the local law.
60. As a consequence, the statutory warranty cannot, by definition, constitute a separate performance obligation and therefore cannot result in the recognition of revenue. The accounting treatment of the statutory warranty, in accordance with IAS 37, should be maintained.

Question 5: Do you agree that an entity should separate the performance obligations in a contract on the basis on when the entity transfers the promised assets to the customer? Why or why not? If not, what principle would you specific for separating performance obligations?

61. As discussed in our answer to question 4, the CNC considers that the segmentation approach proposed in the DP might result in its complexity outweighing its potential benefits and questions the usefulness of the information provided when a separate performance obligation does not correspond to a good or a service that has a standalone value for the customer or does not reflect the economic effects of the transaction. The CNC considers that the proposal of the DP to separate performance obligations in a contract on the basis of when the entity transfers the promised assets to the customer is not sufficient. Consequently, the CNC encourages the IASB to assess whether other criteria should be taken into account in this process.

Question 6: Do you think that an entity's obligation to accept a returned good and refund the customer's consideration is a performance obligation? Why or why not?

62. The CNC considers that an entity's promise to provide a return right to a customer is not a performance obligation and that a right of return represents a failed sale.
63. In addition, as mentioned in DP 3.41, the CNC considers that when an entity has homogeneous transactions that give it the ability to estimate the proportion of the goods that are likely to be returned (ie the proportion of sales that are likely to fail), the entity would recognise revenue for the proportion of transactions that the entity expects not to fail.

Question 7: Do you think that sales incentives (e.g. discounts on future sales, customer loyalty points and 'free' goods and services) give rise to performance obligations if they are provided in a contract with a customer? Why or why not?

64. The CNC observes that the question is extremely open. A very large number of transactions may correspond: awards granted in connection with an initial sale, outside of an initial sale, related or not to a future sale of a product of the entity.

65. Characterizing what differentiates a sales incentive from a marketing cost, or even from a discount granted at the date of the initial transaction is complex. However, this distinction is fundamental because these transactions do not necessarily follow the same accounting treatment under IFRS.
66. In addition, as already indicated in our comment letter on the proposed interpretation which became IFRIC 13, the CNC considers that where the award does not represent a product or service normally sold in the course of an entity's business it may have the characteristics of a marketing cost and should be treated under IAS 37.
67. As regards the two examples discussed in the DP, the CNC concludes that the gift card and the discount are separate performance obligations.
68. Nevertheless, as discussed below in § 60, the CNC is not of the view that it should systematically result in a separate accounting of such performance obligations.

Question 8: Do you agree that an entity transfers an asset to a customer (and satisfies a performance obligation) when the customer controls the promised good or when the customer receives the promised service? Why or why not? If not please suggest an alternative for determining when a promised good or service is transferred.

#### **Q8.1 - General comment**

69. Defining control is complex, as shown by the discussions held on the framework, consolidation or derecognition projects. However, the CNC considers that defining it and identifying its characteristics consistently in the various IASB projects is essential to avoid any misinterpretation when applying it.
70. The CNC is not convinced that this principle has been sufficiently worked through in the DP so that it can be understood correctly and interpreted in a consistent manner. As a result, the CNC considers that its application would probably not improve the comparability and understandability of revenue for users, which is the overall objective of the DP.
71. In addition, the CNC observes that the Framework project may lead to the removal of the control principle in the definition of an asset. The topic is briefly discussed in the DP when considering that the existing and future definitions of an asset are consistent. Obviously, this discussion is not sufficiently robust. The CNC recommends that the IASB assess the potential effects of this change on the revenue recognition project more thoroughly.

#### **Q8.2 – Control of a good**

72. We noted during our discussions with our constituents that defining control of a good is complex: does it mean to take physical possession of the good? to have the legal title of the good? to control its economic benefits? Does it require all these elements or only some of them (not to say other elements)?

73. It is therefore essential that the IASB develops appropriate guidance on its application. The CNC believes that the indicators illustrating the control of an asset given by IFRIC 18.15 are a good starting point. However, examples illustrating the application of these indicators to complex transactions should be developed. Such complex transactions would be, for instance: sales of goods with repurchase agreements, construction type contracts, consignment stocks or bill and hold agreements. Successfully developing these examples will be a robust test of these indicators.
74. In regard to IFRIC 18.15, the CNC recommends that the IASB clarify the meaning of "generally" in the statement "an entity that controls an asset can *generally* deal with that asset as it pleases." The use of the term suggests that an entity may have control of an asset in some cases without being able to do what it wants with it, which is, again, another illustration of the difficulty of really understanding what control means.

### **Q8.3 - Control of a service**

75. The CNC observes that the IASB acknowledges that considering a service as an asset is not familiar to constituents as outlined in DP 3.13 and following: "Although a service is not typically thought of as an asset, the boards have explained that concept in existing literature". In this respect, the CNC notes that the only example given to constituents to illustrate this concept is that of a very recent standard, namely IFRS 2.
76. It is easy to imagine, and we have noted it in practice, that constituents are even less familiar with the concept of control of a service. In this regard, we have not been able to find any guidance on this topic in existing IFRS.
77. The CNC considers it therefore essential that the IASB defines clearly what the concept of control of a service means and develops targeted guidance and illustrative examples to meet the concerns expressed by constituents in this area. Absent such further work, the CNC is greatly concerned about the possibility for constituents to understand and apply this principle satisfactorily.

### **Q8.4 - Distinction goods / services**

78. The CNC observes that when the contract relates to transactions that combine services and delivery of a good (to a greater or lesser degree):
- a) such as the delivery of a good that implies the provision of a construction service (see the steel girders example in DP 4.39);
  - b) or conversely such as the provision of a service accompanied by the physical delivery of a good (see the report recommending process improvements in DP 4.35),
- applying the control notion is problematic. In addition, this topic is a further illustration of the difficulties in distinguishing between contracts for goods and contracts for services.
79. The CNC also notes that the IASB has not yet succeeded in defining a clear principle in this area. The use of "typically" in the statement "typically a good is an asset that is transferred to a customer at a point in time, whereas a service typically is a continuous transfer of assets to a customer over a period of time" clearly illustrates this fact.



80. When distinguishing between goods and services is difficult, the DP proposes to use indicators such as the level of customization, the payment terms, the right to take over the work in progress or in the case of a home the fact that it is constructed on the customer's land.
81. The CNC notes that none of these indicators is new or decisive. However, the CNC observes that their application will be even more difficult due to the lack of clarity on how they interact with the concepts of control of a good or control of an asset as well as with each other.
82. The DP itself provides a good example of such practical difficulties with respect to the “customer payment terms” indicator:
- a) DP 4.33 mentions "Typically, a customer would not make a non-recoverable payment without receiving an asset in exchange”;
  - b) In contrast, the example 7 "non-refundable upfront payment” considers that the customer does not receive anything in exchange for its upfront payment but without further justifying it.
83. The CNC is concerned that the approach proposed by the DP to distinguish between contracts for a good or for a service will not result in any improvement over existing IFRS practice and even that further difficulties might arise.
84. In addition, more specifically, the CNC recommends that the IASB undertake further work in the area of non-refundable payments. We are not sure that this specific issue, which is particularly complex as noted by the IFRIC during their work on the trailing commissions (topic removed from the IFRIC’s agenda due to its complexity), has been given, at this stage, appropriate attention by the IASB.

#### **Q8.5 - Clarifications concerning service contracts with customers**

85. The CNC also urges the IASB to identify the distinctive characteristics of service contracts and thus to define precisely what a service is.
86. This should help at a minimum:
- a) in analyzing what the appropriate criteria for distinguishing between a contract for good and for a service are,
  - b) in assessing whether the existing criteria used to identify whether a contract is a service contract or a lease contract need to be revisited or completed.

#### **Q8.6 – Analysis of the control in a contract**

87. Identifying who controls the asset and when based on the terms and conditions of the contract may be very complex. In addition, parties to a contract generally seek to protect themselves by requiring specific clauses that have in reality limited effect as long as the contract is executed as planned (for example, a clause requiring the transfer of the asset to the customer in the event of bankruptcy of the entity or a clause of retention of ownership in the event of nonpayment by the customer).
88. The CNC encourages the IASB, once the principles have been clarified to specify that judgment should be applied when analyzing the terms and conditions of a contract so that only substantive terms of the contracts, and not remote clauses, are considered.

Question 9: The boards propose that an entity should recognise revenue only when a performance obligation is satisfied. Are there contracts for which that proposal would not provide decision-useful information? If so, please provide examples.

89. The CNC does not support this proposal. The CNC considers that recognizing revenue only when a performance obligation is satisfied as described in the DP does not provide decision-useful information on the entity's performance in all circumstances. Please refer to our answer to Q1 for further details.

Question 10: In the boards' proposed model, performance obligations are measured initially at the original transaction price. Subsequently, the measurement of a performance obligation is updated only if it is deemed onerous.

(a) Do you agree that performance obligations should be measured initially at the transaction price? Why or why not?

(b) Do you agree that a performance obligation should be deemed onerous and remeasured to the entity's expected cost of satisfying the performance obligation if that cost exceeds the carrying amount of the performance obligation? Why or why not?

(c) Do you think that there are some performance obligations for which the proposed measurement approach would not provide decision-useful information at each financial statement date? Why or why not? If so, what characteristic of the obligations makes that approach unsuitable? Please provide examples.

(d) Do you think that some performance obligations in a revenue recognition standard should be subject to another measurement approach? Why or why not? If so, please provide examples and describe the measurement approach you would use.

#### **Q10.1 - Measurement of the net liability that corresponds to the net position of the contract**

90. As discussed in our answer to question 1, the CNC believes that the entity should recognize a liability only if its obligations under the contract are higher than those rights under this contract (which is different from the proposal made by the IASB in the DP).

91. In such a case, the CNC considers that this liability should be measured as the difference between the cash received from the customer and the amount corresponding to the part of the contract performed by the entity measured at the original transaction price.

Example: suppose that Entity A enters into a contract is for a specific asset with a customer for a transaction price of 100 CU. At the reporting date, 50% of the contract is executed and the customer paid in advance 60 CU. The liability recognized in the statement of financial position is measured as the difference between the cash received from the customer (60 CU) and the amount corresponding to the asset transferred to the customer measured at the original transaction price (50 CU) e.g. 10 CU.

### **Q10.2 - Measurement of the components of a contract**

92. As discussed in our answer to question 4, the CNC considers that the segmentation approach proposed in the DP might result in its complexity outweighing its potential benefits and questions the usefulness of the information provided when a separate performance obligation does not correspond to a good or a service that has a standalone value for the customer or does not reflect the economic effects of performance obligations. Consequently, the CNC encourages the IASB to assess whether other criteria should be taken into account in this process. Thus, the CNC prefers to use the term “components of a contract” hereafter to differentiate with the segmentation approach based on the performance obligation proposed by the IASB.
93. Subject to this reservation, the CNC agrees that the components of a contract should be measured according to the method of allocation of the transaction price proposed in the DP (e.g. allocation of the transaction price based on the stand alone selling value of these components).
94. As a consequence, as discussed in our answer to Q1, assuming that the customer has not performed under the contract, when the entity performs a component of the contract, the entity would recognize an asset, measured on the basis of the relative stand alone selling price allocated to this component with the corresponding revenue.

### **Q10.3 - Remeasurement: onerous contracts with customers and alternative measurement approach**

95. According to the DP, a performance obligation is deemed onerous when an entity’s expected cost of satisfying the performance exceeds the carrying amount of that performance obligation. It is therefore obvious that a contract becomes onerous because of its costs and not because of the amount of revenue attached to it.
96. As discussed in our general comment GC3, the CNC considers that issues related to the costs of a contract should not be debated before the scope of this project has been rediscussed with stakeholders.
97. Consequently, the CNC considers that the corresponding provisions of existing IFRSs relating to onerous contracts should be maintained and not reassessed at this stage of the project.

Question 11: The boards propose that an entity should allocate the transaction price at contract inception to the performance obligations. Therefore, any amounts that an entity charges customers to recover any costs of obtaining the contract (eg selling costs) are included in the initial measurement of the performance obligations. The boards propose that an entity should recognise those costs as expenses, unless they qualify for recognition as an asset in accordance with other standards.

(a) Do you agree that any amounts an entity charges a customer to recover the costs of obtaining the contract should be included in the initial measurement of an entity’s performance obligations? Why or why not?

98. As discussed in our answer Q10.1, the CNC believes that the entity should recognize a liability only if its obligations under the contract are higher than those rights under this contract. In such a case, this liability reflects the obligation to perform of the entity for the part of the contract for which the customer has already performed. Thus, this liability does not correspond to the “initial measurement of an entity’s performance obligations” of the DP.

Question 11 (b) In what cases would recognising contract origination costs as expenses as they are incurred not provide decision-useful information about an entity’s financial position and financial performance? Please provide examples and explain why.

99. Overall, the CNC supports the proposal to recognize the contract origination costs as expenses as they are incurred. However, the CNC is not convinced that this proposal will allow for the appropriate representation of performance for all activities, in particular for insurance contracts (see our response to the DP « Insurance Contracts », dated November 16, 2007, question 8).

100. In addition, the CNC recommends that the IASB notes that:

- a) Several terms are used in this question e.g. 'costs of obtaining the contract, selling costs or contract origination costs'. We would like the IASB to clarify if there are any differences in these terms and to give a clear definition of the term that will be retained. Clarifying it will avoid the risk of having different views on the nature of the costs considered in this provision of the DP;
- b) The IFRIC has been questioned recently on the subject of accounting for sales costs in the context of real estate development and has decided not to take the question on this agenda as it was not possible to reach a conclusion on the appropriate accounting for broad categories of selling and marketing expenses;
- c) Question 11 states that some of the costs of obtaining the contract could be recorded as an asset according to other standards but without specifying in which circumstances;

101. In this regard, the CNC recommends that the IASB indicates which costs and standards are concerned so as to ensure that this proposal of the DP is correctly understood and applied.

Question 12: Do you agree that the transaction price should be allocated to the performance obligations on the basis of the entity’s stand alone selling prices of the goods or services underlying those performance obligations? Why or why not? If not, on what basis would you allocate the transaction price?

102. The CNC supports this proposal. However, the CNC considers that the IASB should clarify whether this proposal has any effect on existing IFRS particularly with regard to the application of IFRIC 13 Customer Loyalty Programs or IFRIC 18 ' Transfers of Assets from Customers.

Question 13: Do you agree that if an entity does not sell a good or a service separately, it should estimate the stand-alone selling price of that good or service for purposes of allocating the transaction price? Why or why not? When, if ever, should the use of estimates be constrained?

**Q13.1 - The DP does not specify whether the stand-alone estimated selling price should be determined taking into account the characteristics of the customer with whom the contract is signed**

103. It is not clear in the DP whether the stand alone price used to allocate the transaction price should be determined considering the characteristics of the customer with whom the contract was signed. The example given in DP 5.50 indicates that the price of the product is CU 60 because "SellerCo regularly sells product A separately for CU 60" without providing any additional explanation.
104. This may lead to practical difficulties. Taking the same example, if the entity regularly sells product A separately at a price of CU 60 to a category of customers (eg purchasing large volumes of product A) and of CU 70 to others: what is the appropriate stand alone price selling price? an average price (on which period?), the last prices observed (on which period), the price observed on a portfolio basis?
105. The CNC recommends that the IASB provide guidance to clarify how the stand alone selling price should be determined so that to avoid any differing interpretations.

**Q13.2 - The requirement for entities to consider the stand alone selling price by other entities should be rediscussed**

106. The CNC notes that the question seems to suggest that if the entity does not sell the products it should then estimate the stand alone selling price without having to perform additional steps.
107. However, if the entity does not sell the products separately, based on DP 5.46, we understand that the entity must search for the price charged by other entities for the same goods and services sold separately before having the possibility to use its own estimates.
108. The CNC would like the IASB to reconsider the costs/benefits reasons of this requirement: is it possible in practice (and legally permissible) for entities to obtain reliable and comparable data? how would an entity document that it has performed this search for its auditors? What will the value of the information provided be, compared to an estimation of the stand alone selling price performed by the entity?
109. Therefore, the CNC invites the IASB to expose the reasons for this requirement and to reconsider the circumstances in which it should be applied, for example, it might be only if this information is reasonably available without undue cost and effort?