

## BELGIAN ACCOUNTING STANDARDS BOARD



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Our reference  
**C-070**

Your reference

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Dear Sir, Madam,

The Belgian Accounting Standards Board (BASB) would like to comment on EFRAG's Draft Comment Letter on the Discussion Paper *Preliminary Views on Revenue Recognition in Contracts with Customers*.

Although we support the development of a fully converged revenue standard, based on one single set of principles for recognition and measurement applicable to all types of revenue-generating activities, this seems us a very difficult objective. Our concerns are explained in the answers to the questions below.

The approach to recognize revenue only when the performance obligation arising under a contract with a customer is satisfied seems us rather rigid. The proposal stipulates that the satisfaction will occur when control of the asset (a good or a service) involved is transferred to the customer. This will result in a significant change in timing of revenue recognition when contracts for construction (within the scope of IAS 11) and/or services are involved and no continuous transfer takes place (since it will result in the withdrawing of the percentage of completion method). In our view, for some industries, the transfer of the significant risks and rewards of ownership to the buyer should, again, be emphasized in the recognition process of revenue. These risks are often of an economical nature and not linked to physical control.

The discussion paper also seems to suggest that service contracts typically involve a continuous transfer, but we share the view of EFRAG that in many service contracts the deliverable is delivered at the end of the contract (es. due diligence contracts, some contract research). We wonder what will be the consequences of the proposed approach for this kind of services.

Our detailed comments on the questions can be summarized as follows.

### **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?***

We agree that a single, universally applied revenue recognition principle is preferable to having two different revenue recognition standards (IAS 11 and IAS 18). However, the application of only one single revenue recognition principle will be very difficult for different types of transactions and will not always provide decision useful information to the users and will not reflect management view.

Although we accept the importance of the changes in contract assets and liabilities while recognizing revenue, in our view, revenue should not only be recognized when a performance obligation is satisfied. The recognition of revenue should in many circumstances be based on the different activities carried out to fulfill contracts with customers.

### **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?***

The BASB is of the opinion that for long term contracts such as contracts for construction or contracts where no continuous transfer of assets takes place, the proposed principle will not provide in decision-useful information for the management. As stated in paragraph 22 of IAS 11 (when the outcome of a construction contract can be estimated reliably), contract revenue and contract costs associated with the construction contract shall be recognized as revenue and expenses respectively by reference to the stage of completion of the contract activity at the end of the reporting period. Based on the management-approach, only the use of the "percentage of completion method" shall, for those kinds of contracts, provide decision-useful information also for the users.

### **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.***

We agree defining a contract as "an agreement between two or more parties that creates enforceable obligations". However, we think that it is important that the IASB explains the term "enforceable" (ref IAS 32.13).

#### **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.***

The BASB agrees with the definition of a performance obligation.

#### **Question 5**

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

Performance obligations can be satisfied at different times. The objective is to ensure that an entity's revenue faithfully represents the pattern of satisfaction of performance obligations. It is only when the performance obligations are satisfied at different times that separation is required to depict faithfully the changes in the performance obligations over the life of the contract.

For the BASB it is not clear what is meant with 'the satisfaction of performance obligations at different times'. Does this mean a separate transfer of assets? How are promised assets (such as maintenance services) dealt with? In the discussion paper, the transfer of the significant risks and rewards of ownership has been replaced by the transfer of control of the asset to the customer. But the customer himself is not always able to determine the transfer of the assets (es. maintenance services).

#### **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?***

Yes, the BASB considers a customer's right to return the goods 'bought' for any reason as a separate performance obligation. The right to return is a service that is transferred to the customer. Sometimes customers pay even a premium for this service. This means that the part of the consideration received from the sale that includes the right to return needs to be allocated to the performance obligation relating to the return right and should not be recognized as revenue until that performance obligation is satisfied (until either the right is exercised or expires).

#### **Question 7**

***Do you think that sales incentives (eg 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?***

We agree with paragraph 3.32. In the first example, the customer receives a gift card with the purchase of a music player. The customer can redeem the gift card by downloading music. In the second example, the customer receives a discount on a future purchase of online music with the purchase of a music player.

In our view, the promise to transfer music to a customer at a discount is not a performance obligation, because the customer must pay additional consideration to obtain the online music. The promised discount relates to a future contract and can not be a performance obligation in the existing contract (the purchase of the music player).

In the gift card example, the gift card is a separate performance obligation. The customer is not required to pay additional consideration to obtain the online music. The customer receives an unconditional and enforceable right to download a certain amount of music. That right could be sold separately.

### **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.***

The BASB does not agree with the proposal that a performance obligation is satisfied only when the assets has been transferred to the customer. An asset is said to be transferred to a customer when the customers controls it. The BASB wants to underline the importance of the 'risk and awards test', as currently explained in IAS 18. Especially for some industries, such as the real estate industry, the application of the control-based test will not provide decision-useful information to the management.

Also the propositions IFRIC 15 Agreements for the Construction of Real Estate should be reconsidered.

### **Question 9**

***The boards propose that an entity should recognize 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.***

The BASB has, like EFRAG, some concerns with the proposed approach. The application of the revenue recognition principle in the discussion paper could result in a significant change to the existing practice, with the recognition of revenue occurring much later than the present on construction-type contracts and services contracts. The BASB doubts whether this accounting effect will result in more decision-useful information than the existing standards.

Remark concerning paragraph 4.30: In practice, wouldn't the buyer have obtained contractual protection that, if the seller were to breach the contract subsequently to the delivery of X and Y, X and Y can be returned? So even though the buyer may control, he will not bear substantially all risks and rewards.

### **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.*

The BASB is of the opinion that the rights arising under the contract should be measured at an amount equal to the transaction price: the value of the consideration to be received. Also the performance obligations should, at contract inception, be measured at an amount equal to the transaction price (the original transaction approach).

Because, at contract inception, the rights and performance obligations in the contract will be measured at the same amount, no revenue will be recognized at that point.

According to the model proposed in the discussion paper, the initial measurement of a performance obligation should not consequently be updated unless the performance obligation has been satisfied or the obligation is deemed onerous. A performance obligation is deemed onerous when the expected costs of satisfying that performance obligation exceeds its carrying amount.

The BASB also agrees with the proposal in the discussion paper that a performance obligation that is deemed onerous should be remeasured to the entity's expected cost to satisfy the performance obligation.

The BASB wants to repeat that it is very difficult to have one single, universally-applicable revenue recognition principle. Besides, a revenue recognition principle that involves 'recognizing revenue as the contract progresses' still seems for the BASB a solid revenue recognition principle, in case of individualized goods or services for which the client bears the major economical risks.

Also more guidance on subsequent measurement related to contract renegotiation should be foreseen by the standard.

Remark concerning paragraph 5.43: The standard should provide more guidance in case of a contract with a fixed price per unit, but when the number of units has not been determined in the contract.

### **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 recognize 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?***

***(b) In what cases would recognizing 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.***

According to the proposed model, a performance obligation is, at contract inception, measured at an amount equal to the transaction price. This is also the amount at which the rights are measured. Consequently, at contract inception no revenue is recognized. The whole of the revenue will be attributed to the fulfillment of future obligations (which is in line with the matching principle).

The BASB agrees that pre-contract costs incurred on entering into the contract should be expensed immediately. Consequently, other standards should be adjusted in this way.

### **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?***

If there is more than one performance obligation in a contract and it is necessary to unbundle the contract into the underlying performance obligations, the total transaction price should be allocated to the individual performance obligations.

Although the BASB agrees with this proposal, we think that not all performance obligations are separable into smaller components.

We also agree with Efrag's observation that the stand-alone selling prices ought to be readily available and the used method ought to be relatively simple to apply.

### **Question 13**

***Do you agree that if an entity does not sell a good or 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?***

Isn't the lack of market based evidence indicative there's no separate performance obligation? (Example 1: Multiple-element arrangement; A5: 'Evidenced by the fact that other entities sell such services separately').

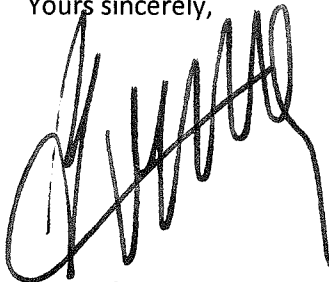
Nevertheless, the BASB agrees that, for purposes of allocating the transaction price, if an entity does not itself sell a good or service separately, it should estimate the price for which it would sell the good or service to its customers.

An entity can use various methods to estimate a stand-alone selling price of a promised good or service. Suitable estimation methods include:

- the expected cost plus a margin approach; and
- the adjusted market assessment approach.

If you have any questions concerning our comments, please do not hesitate to contact us.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'Jan Verhoeye', written in a cursive style.

Jan Verhoeye  
Chairman