IFRS Accounting

Staff paper

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Project	**Post-implementation Review of IFRS 15**
Topic	**Analysis of outreach feedback—Requirements for the five steps of revenue recognition**
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Purpose and structure

1. This paper is the second of four papers analysing feedback from phase 1 outreach on the post-implementation review (PIR) of IFRS 15 *Revenue from Contracts with Customers*. Specifically, the paper summarises feedback on the requirements for the five steps of the revenue recognition model:

   (a) Step 1: Identifying the contract(s) with a customer (paragraphs 5–18);

   (b) Step 2: Identifying the performance obligations in the contract (paragraphs 19–36);

   (c) Step 3: Determining the transaction price (paragraphs 37–68);

   (d) Step 4: Allocating the transaction price to the performance obligations in the contract (paragraphs 69–74); and

   (e) Step 5: Recognising revenue when (or as) the entity satisfies a performance obligation (paragraphs 75–87).

2. For each area, the paper provides staff analysis and recommendations on whether to cover the area in the request for information (RFI) and if so, which matters to ask questions about. The areas not covered by specific questions in the RFI will be covered by a general catch-all question.

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3. Agenda Papers 6D–6E for this meeting analyse feedback on other areas of the IFRS 15 requirements and on the interaction between IFRS 15 and other IFRS Accounting Standards.

Summary of staff recommendations

4. The staff recommend the IASB ask questions in the RFI about the following matters:

   (a) *identifying the performance obligations in a contract*:

      (i) fact patterns in which requirements are applied inconsistently, lead to outcomes not reflecting the underlying economic substance or lead to significant ongoing costs.

   (b) *determining the transaction price*:

      (i) diversity in practice in the presentation of consideration payable to a customer, in particular in relation to incentives paid by an agent to the end consumer and incentives that exceed revenue from a contract; and

      (ii) diversity in practice in the presentation of sales-based taxes.

   (c) *determining the timing of revenue recognition*:

      (i) fact patterns in which the guidance is unclear or may be applied inconsistently, in particular when applying the criteria for over time revenue recognition.

Questions for the IASB

Questions for the IASB
1. Do IASB members agree with the staff recommendation in paragraph 4 of this paper? 2. Are there any additional matters related to the requirements for the five steps of the revenue recognition model that the IASB should seek feedback on in the request for information?

Step 1: Identifying the contract(s) with a customer

Background

5. IFRS 15 defines a contract as an agreement between two or more parties that creates enforceable rights and obligations.

6. Paragraph 9 sets out the criteria that must be met for a contract to be accounted for applying IFRS 15, including that it should be probable that the entity will collect the consideration to which it will be entitled to in exchange for the promised goods or services (collectability criterion).

7. If a contract does not meet the criteria in paragraph 9 and an entity receives consideration from the customer, the consideration will be recognised as revenue only when:

   (a) the entity has no remaining obligations to transfer goods or services and the consideration is non-refundable; or

   (b) the contract has been terminated and the consideration is non-refundable.

8. Paragraphs 18–21 set out the requirements for accounting for contract modifications. A modification is accounted for as a separate contract if the added promised goods or services are distinct and increased consideration reflects their stand-alone selling prices. In other cases, the modification is accounted for:

   (a) as if it were a termination of the existing contract and the creation of a new contract—if the remaining goods or services are distinct from those already transferred; or

   (b) as if it were part of the existing contract with a cumulative catch-up adjustment to revenue—in remaining cases.

Overview of feedback

9. We did not receive much feedback on this area.

10. Some stakeholders, including preparers, accounting firms, standard-setters and regulators, commented on challenges related to accounting for contract modifications.

11. The main challenge identified related to deciding between the three methods for accounting for contract modifications, including assessing whether the added goods or services are distinct. Stakeholders said that determining how to account for contract modifications is challenging because many modifications are unique and require entities to exercise significant judgement. Some stakeholders said that most of the challenges in this area have been overcome—entities have developed accounting policies for common modifications that provide a good basis for deciding which of the three methods apply. However, a few stakeholders expressed concern that:

    (a) there may be some diversity in practice in accounting for contract modifications, for example, in the construction industry.

    (b) some of the guidance on contract modification is unclear, for example, the guidance on allocating the consideration included in a modification but related to the goods or services already transferred by an entity. A few preparers suggested that applying the guidance in paragraph 21(a) may sometimes lead to allocation of consideration to the remaining promised goods or services which in their view would not reflect the substance of the transaction.

12. In addition, a few respondents raised the following matters:

    (a) an accounting firm and a few national standard-setters raised questions on accounting for upfront non-refundable payments related to contracts that do not meet the criteria in paragraph 9 of IFRS 15. For example, they asked how to account for an upfront non-refundable payment from a customer on a framework contract without minimum purchase obligation, including on the termination of such contract.

    (b) an accounting firm raised a question on distinguishing between variable consideration and contract modifications, for example, whether changes that do not obviously change a scope or a price of a contract such as changes to triggers for variable consideration could represent contract modifications.

(c) an accounting firm raised a question specific to licence renewals (see paragraph 31(d)(ii) of Agenda Paper 6D).

13. Stakeholders did not provide any specific suggestions for resolving the matters mentioned in paragraphs 11–12, except for considering the guidance on licence renewals published by the FASB (see paragraph 32(c) of Agenda Paper 6D).

Staff analysis and recommendations

14. We received relatively little feedback on the requirements and guidance related to Step 1. The feedback suggests that most issues related to contract modifications have now been resolved.

15. The remaining challenges and suggested diversity in practice seem to relate mostly to determining whether the goods or services promised by a contract modification are distinct, and so relate to the guidance on identifying the performance obligations in a contract (see paragraph 23).

16. In respect to the matters mentioned in paragraph 12, the staff note that:

(a) paragraphs 15–16 of IFRS 15 provide guidance on recognising non-refundable consideration received from a customer as revenue, including in case of contract termination; and

(b) the issue mentioned in paragraph 12(b) is likely to affect only a small proportion of contracts and is unlikely to lead to material effect on entities' financial statements.

17. In addition, stakeholders did not provide specific suggestions for improving the guidance on Step 1 of the revenue recognition process, including on accounting for contract modifications.

18. For the reasons in paragraphs 14–17, the staff recommend not including in the RFI a specific question on the requirements for Step 1: Identifying the contract(s) with a customer.

Step 2: Identifying the performance obligations in the contract

Background

19. A performance obligation is a promise in a contract with a customer to transfer to the customer either:

    (a) a good or service (or a bundle of goods or services) that is distinct; or

    (b) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.

20. The IASB's objective in developing the concept of a performance obligation was to ensure that entities appropriately identify the unit of account for the goods and services promised in a contract. The five-step revenue recognition model is an allocated transaction price model, so identifying a meaningful unit of account is fundamental to recognising revenue on a basis that faithfully depicts the entity's performance in transferring the promised goods or services to the customer.

21. In determining whether a good or a service is distinct, an entity considers if the customer can benefit from the good or service on its own or together with other resources that are readily available to the customer. The entity also considers whether its promise to transfer the good or service to the customer is separately identifiable from other promises in the contract.[1]

Overview of feedback

22. Many stakeholders of all types commented on application matters related to identifying the performance obligations in a contract. The comments related to:

    (a) challenges applying specific requirements for Step 2; and

[1] See paragraph 27 of IFRS 15.

(b) cases when applying the requirements may result in outcomes that do not reflect the economics of a transaction or lead to significant costs.

Challenges in applying specific requirements

23. Many stakeholders said that identifying the performance obligations in a contract is challenging, mostly because decisions involve significant judgement. Stakeholders highlighted application matters related to:

(a) identifying a good or service specified in a contract, including:

(i) determining whether a company promised to provide a good or a service or a right to a good or a service. A few stakeholders suggested that in some cases the determination may lead to a different accounting outcome, for example, it may affect whether the entity has transferred control.

(ii) identifying the offerings in some digital solutions, for example, determining what is being offered on a digital platform (a right to use the platform, tokens to use the platform, widgets sold on the platform?) or determining whether a cryptocurrency is a good or a service.

(b) applying the concept of 'distinct' to determine whether a separate performance obligation exists, including:

(i) in relation to internally developed products;

(ii) for bundles of services or for bundles of goods and services (for example, are services offered in a software as a service (SaaS) arrangement, such as access to cloud-based software, its updates and security services, distinct?);

(iii) for contract modifications;

(iv) in licensing and out-licensing arrangements; and

(v) in arrangements with principal versus agent considerations.

24. A few stakeholders said there may be diversity in practice related to applying the requirements on identifying performance obligations, in particular in the software and construction industries.

25. A few stakeholders, including some preparers and accounting firms, said that although the transition to IFRS 15 was challenging, many entities have developed policies and procedures for identifying performance obligations and for documenting the related judgements—new questions arise mostly in relation to new business developments.

26. Stakeholders had mixed views on resolving the matters mentioned in paragraph 23:

    (a) some stakeholders suggested providing more application guidance or illustrative examples on specific issues, for example on separating physical and digital aspects in a bundle or on distinguishing whether a promise in a contract is to provide a good or a service or a right to a good or a service.

    (b) a few stakeholders, including a few accounting firms and a regulator said that these are application matters resulting from the need to apply judgement to often complex contracts. In their view, amending guidance on Step 2 would require entities to review their existing accounting policies and cause disruption, and so would be unlikely to meet the cost-benefit test.

    (c) a few accounting firms suggested that to improve consistency in making judgements, the IASB should include in IFRS 15 some of the guidance from the Basis for Conclusions on the Standard and from materials supporting the application of the Standard. For example, they suggested that the discussion on considering whether there is a 'transformative relationship' between the two items in the process in the IFRS Interpretations Committee (IC) agenda decision *Revenue recognition in real estate contract that includes the transfer of land* and the discussion on 'separable risks' in paragraphs BC105 and BC116K of the Basis for Conclusions often help entities make judgements. However, these discussions may be overlooked by preparers who are less familiar with the Standard and materials supporting its application.

27. In addition, an accounting firm expressed a view that some entities are considering the way in which a customer expects to use the goods or services rather than the entity's promises in the contract when assessing whether they have a single or multiple performance obligations. The firm suggested this may lead to diversity in practice, in particular in the software and construction industries. They suggested the IASB consider clarifying in the Standard whether and how the customer's expectation that it would receive a single deliverable should affect the entity's assessment of its performance obligations in a contract.

Requirements that may result in outcomes not reflecting the economics of a transaction or in significant costs

28. A few stakeholders gave examples of fact patterns, in which separating performance obligations as required by IFRS 15 leads to outcomes that in their view do not reflect the economics of the transaction. For example:

    (a) a regulator gave an example of a property developer that sells apartments with various facilities such as green spaces and a swimming pool. The facilities take longer to complete than the apartments and on completion are transferred to a legal entity owned by members of the community that will manage the facilities on their behalf. In this case, the developer disagreed with its auditors who suggested identifying separate performance obligations for the transfer of the apartments and facilities because the developer sees the sale as one transaction.

    (b) a few preparers suggested that unbundling a sale of a handset from airtime services does not reflect the economics of the transaction and may lead to a mismatch of revenue and expenses because the preparers see the sale of discounted handsets as a tool to get clients to sign up for the services. In addition, some telecommunication companies said that users of their financial statements continue to ask for non-GAAP performance measures, such as customer acquisition cost or average revenue per user, that were used before IFRS 15 was implemented.

29. Stakeholders mentioned in paragraphs 28(a)–28(b) suggested that the IASB consider a simplified approach that would allow for flexibility in identifying the performance obligations in 'economically bundled contracts' or for goods and services provided at the same time and for the same or similar period.

30. A few preparers expressed concern that in some cases the costs of identifying and accounting for separate performance obligations exceed the benefits of doing so, for example, in separating freight services from the sale of goods or separating property services from the lease of real estate. In some cases, preparers account for a single performance obligation rather than several because the effect on the financial statements would be immaterial but they say it is costly to go through the process of gathering evidence that the effect would be immaterial. A few preparers suggested the IASB should consider providing a practical expedient for insignificant components of contracts.

Staff analysis and recommendations

31. The feedback in paragraph 23 highlights matters that require the application of judgement with many of the provided examples relating to complex transactions involving provision of new types of goods and services.

32. Therefore, there is a question whether the diversity in practice mentioned in paragraph 24 is due to the specifics of the contracts, or whether the diversity is caused by unclear or insufficient guidance. In our view, gathering further information about circumstances in which entities are unclear how to apply the requirements on identifying performance obligations and in which they observe diversity in practice, will help the IASB assess whether the effects of the requirements are as expected and whether requirements are capable of being applied consistently. This information will also provide evidence on the cause of any diversity in practice, the prevalence of any diversity, and the effects of any diversity.

33. The staff think the examples reported in paragraph 28 highlight cases where the outcome of applying the requirements on identification of performance obligations

seems to differ from the management's view of the transaction. While the requirements in IFRS 15 were not intended to provide management's view of transactions, we think that it would be helpful to gather further evidence of cases in which stakeholders think the outcomes do not reflect the underlying economics of the transaction. This will help the IASB assess the cause and the pervasiveness of such cases.

34. The staff also acknowledge the concerns related to high costs of applying the requirements on identifying performance obligations in some fact patterns (see paragraph 30). Both examples provided by stakeholders relate to matters which were considered by the Transition Resource Group (TRG). Following the TRG discussions the FASB issues amendments related to these matters (see items 6 and 7 in Appendix A of Agenda Paper 6A). The IASB did not make similar clarifications because:
    (a) permitting an accounting policy choice for shipping and handling activities after control of the goods has been transferred to the customer:
        (i) would create an exception to the revenue recognition model and potentially reduce comparability between entities; and
        (ii) would apply to all entities, consequently, it is possible that entities with significant shipping operations would make different policy elections.[2]
    (b) introducing a clarification for items immaterial in the context of the contract was considered unnecessary given the overall objective of IFRS 15 and the overarching concept of materiality in IFRS Accounting Standards.[3]

35. However, we think that gathering further examples of fact patterns in which applying the requirements on identifying performance obligations leads to significant costs would help the IASB assess the pervasiveness of these cases.

[2] See paragraph B116U of the Basis for Conclusions on IFRS 15.
[3] See paragraphs BC116C–BC116E of the Basis for Conclusions on IFRS 15.

36. For the reasons in paragraphs 31–35, the staff recommend including in the RFI a question related to the guidance on identifying the performance obligations in the contract, focusing on identifying fact patterns in which the requirements are applied inconsistently, lead to outcomes not reflecting the underlying economic substance or lead to significant ongoing costs.

Step 3: Determining the transaction price

Background

37. The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties (for example, some sales taxes).

38. IFRS 15 also provides specific requirements for determining the transaction price if consideration includes a variable amount, a significant financing component or any consideration payable to the customer.

39. Variable consideration is estimated using either the expected value or the most likely amount method. Some or all of the estimated amount of variable consideration is included in the transaction price only to the extent it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur when the uncertainty associated with the variable consideration is subsequently resolved.[4]

40. The promised amount of consideration is adjusted for the effects of the time value of money if the timing of payments provides the customer or the entity with a significant benefit of financing. As a practical expedient, an entity need not adjust the consideration if at contract inception the entity expects that the period between the

[4] See paragraphs 53–59 of IFRS 15.

entity transferring goods and services and the customer paying will be one year or less.[5]

41. Consideration payable to a customer is accounted for as a reduction of the transaction price unless the payment is in exchange for a distinct good or service from the customer.[6]

Overview of feedback

42. Many stakeholders of all types commented on application matters related to determining the transaction price. The comments related to:

    (a) variable consideration;

    (b) consideration payable to a customer;

    (c) significant financing component; and

    (d) other guidance on determining the transaction price.

Variable consideration

43. Some stakeholders, mainly preparers, commented on challenges related to applying the requirements on accounting for variable consideration. The main matter raised was the difficulty in providing estimates for variable consideration for performance obligations with outcomes outside of the entity's control, for long-term performance obligations and in cases when an entity enters a new market or starts providing a new good or service the success of which is uncertain.

44. Stakeholders gave some examples of arrangements in which estimating variable consideration is challenging, including:

    (a) trailing commissions in the asset management sector when fees are calculated as a percentage of the value of investments in a fund;

[5] See paragraphs 60–65 of IFRS 15.

[6] See paragraphs 70–72 of IFRS 15.

(b) variable consideration in long-term contracts in the oil and gas sector based on throughput;

(c) variable consideration in long-term SaaS contracts; and

(d) variable royalties-based revenue in the media industry based on estimates of music being played in various locations (this issue is further complicated by uncertainty about whether and when the music is played).

45. Stakeholders said that the high level of uncertainty related to these fact patterns makes it is difficult for entities to estimate the variable consideration initially and may lead to significant adjustments in the future. A national standard-setter suggested that the significant level of judgement required to estimate variable consideration in for example the construction industry may lead to some diversity in practice. However, some stakeholders said that practice has developed in this area and significant reversals of amounts recognised related to variable consideration are rare.

46. A few stakeholders expressed concerns about applying the guidance on constraining estimates of variable consideration:

(a) a preparer and an accounting firm said that entities may be interpreting the 'highly probable' [that a significant reversal will not occur] threshold differently and may seek different levels of evidence to support their estimates;

(b) an accounting firm said there is a tendency to constrain an estimate of variable consideration to zero for very long-term contracts; and

(c) a standard-setter questioned the suitability of recognising any revenue for variable consideration that depends on the customer's future actions.

47. Other suggestions were made by one stakeholder each:

(a) to broaden the scope of the exception in paragraph B63. This paragraph currently applies to licences of intellectual property for which the consideration is based on the customer's sales or usage and requires an entity not to recognise any revenue for the uncertain amounts until the uncertainty is resolved (ie when the customer's subsequent sales or usage occurs).

(b) to include some of the supporting guidance and examples related to estimating variable consideration in the Standard itself. At the moment it is challenging to explain some reductions in estimated transaction price if the reductions are made considering, for example, IC agenda decisions such as *Compensations for Delays and Cancellations*.

(c) to provide more guidance on distinguishing between amounts payable to a customer and variable consideration.

Consideration payable to a customer

48. Some stakeholders, mainly accounting firms and preparers, raised matters related to accounting for consideration payable to a customer, including:

(a) identifying whether consideration payable to a customer is for a distinct good or service. For example, preparers asked how to treat slotting fees paid in the retail industry, fees for digital advertising paid to platform entities that are also the entity's customer, and payments for goods or services acquired from a customer to be used as an input into production. Preparers who raised the matter said that they have developed accounting policies in these areas but were unsure whether their policies are consistent with other entities.

(b) accounting for incentives offered in triangle arrangements when a party acting as an agent provides a marketing incentive to end consumers—can these incentives be seen as payments to a customer and should they be presented as a reduction of revenue or as a marketing expense? Stakeholders said that this matter is common in the technology, telecommunications and media industries, the amounts may be material and there is diversity in practice. A user also noted that differences in presentation complicate their analysis. Stakeholders suggested clarifying the guidance in IFRS 15, including by incorporating in the Standard some of the TRG discussions on this topic.

(c) accounting for 'negative revenue' when consideration payable to a customer exceeds revenue earned from the customer. Stakeholders said that this matter

is common when entities try to enter a highly competitive market and offer large incentives to consumers. Stakeholders suggested that there is diversity in practice with some entities presenting negative revenue and others reclassifying the amounts of incentives exceeding revenue as expenses. An accounting firm noted that a similar issue may arise in relation to other types of variable consideration and noted that in its agenda decision *Compensations for Delays or Cancellations* the IC decided not to consider the question of whether the amount of compensation recognised as a reduction of revenue is limited to reducing the transaction price to nil. Stakeholders suggested the IASB should clarify how to present net revenue that is negative. In addition, they asked:

(i) what would be the unit of account for assessing net revenue—should the entity make an assessment on a contract-by-contract basis or on a portfolio basis?

(ii) what should be the period for the assessment? For example, consideration payable to a customer may exceed revenue in year 1 but be lower than revenue expected to be earned over the term of the contract.

(iii) how to account for any reversals if a contract starts performing better in future periods?

Significant financing component

49. We received little feedback on this topic. A few stakeholders asked for clarifications on the following matters:

(a) an accounting firm asked whether the discount rate used for adjusting the promised amount of consideration for a significant financing component should be adjusted when a contract is modified.

(b) another accounting firm asked whether an entity should assess whether a significant financing component exists based on the contract as a whole or based on the separate performance obligation it relates to.

(c) a few stakeholders from Latin America suggested that high inflation in a jurisdiction should be considered in accounting for a significant financing component. Their suggestions included removing the one-year threshold for a practical expedient or leaving it to entities' judgement because in their view the current threshold for applying the relief may result in an unfair presentation of the transaction price and may worsen comparability between entities in jurisdictions with high inflation and high interest rates.

50. A few telecommunications companies also raised a question on the interaction between the requirements for significant financing component in IFRS 15 and the requirements for accounting for expected credit losses (see paragraphs 16–17 in Agenda Paper 6E).

Other guidance on determining the transaction price

51. A few respondents asked for clarifications on other areas of guidance on determining the transaction price, including:

(a) non-cash-consideration—an accounting firm asked what should be the measurement date for the fair value of the non-cash consideration, noting that Topic 606 states that this is the date that the contract is entered into.

(b) sales-based taxes—an accounting firm asked the IASB to provide more guidance on determining whether an entity is collecting tax on behalf of the tax authority or whether it is responsible for paying the tax itself. This determination affects whether the entity should include the tax in determining the transaction price or exclude it from the transaction price. The stakeholder said that the amounts involved may be material and that there is diversity in practice not only between jurisdictions (which may be caused by differences in tax legislation) but also between entities within the same jurisdiction.

Staff analysis and recommendations

Variable consideration

52. The staff note that most issues mentioned in paragraphs 43–44 relate to challenges with exercising judgement in conditions of high uncertainty. However, estimating variable consideration inherently requires the exercise of judgement. Stakeholders did not provide any suggestions for improving or clarifying the guidance and it is unlikely that the IASB will be able to develop further guidance to make the estimation process easier. In addition, we note that the feedback received suggests that despite initial challenges entities have developed accounting policies for estimating variable consideration and there is no evidence of significant diversity in practice.

53. The feedback from users at the time of developing the Standard indicated that the most relevant measure for revenue in a reporting period would be one that will not result in a significant reversal in a subsequent period. Phase 1 feedback from preparers does not indicate significant reversals in subsequent periods. We have not heard concerns from users relating to variable consideration.

54. In response to respondents' concerns related to the guidance on constraining estimates of variable consideration and other feedback in paragraphs 46–47, the staff note that:

    (a) the 'highly probable' threshold used in IFRS 15 had already been used in IFRS Accounting Standards. IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* defined 'probable' as 'more likely than not', and 'highly probable' as 'significantly more likely than probable'. To help entities apply the threshold, IFRS 15 provides guidance on factors that could increase the likelihood or the magnitude of a revenue reversal and so in some cases may lead to entities constraining variable consideration to zero. In addition, paragraph 126 of IFRS 15 requires entities to disclose information about the methods, inputs and assumptions used for estimating variable consideration and assessing whether the estimate is constrained.

(b) paragraphs BC415–BC421 of the Basis for Conclusions explain the IASB's reasons for providing the exception for sales-based and usage-based royalties in paragraph B63 and for retaining the scope of the exception—both users and preparers of financial statements indicated that significant adjustments during the contract term to the amount of revenue recognised at inception of the contract would not provide useful information because they would not relate to the entity's performance. Phase 1 feedback does not indicate any concerns from users or preparers related to significant reversals of revenue in relation to other types of contracts.

(c) the suggestions in paragraphs 47(b)–47(c) were made by one stakeholder each and do not suggest significant problems with the IFRS 15 requirements.

55. For the reasons mentioned in paragraphs 52–54, the staff recommend not including in the RFI a specific question related to variable consideration.

Consideration payable to a customer

56. The first matter raised in paragraph 48(a) relates to applying the concept of 'distinct' in identifying performance obligations—in paragraph 36 the staff recommends exploring this matter in the RFI.

57. The matter raised in paragraph 48(b) relates to determining whether payments made to customers' customers are within the scope of paragraph 70 of IFRS 15 which sets out the requirements for accounting for consideration payable to a customer. The TRG discussed the issue of whether entities should consider entities in the distribution chain in assessing whether payments to customers are present but did not definitively conclude on this question.

58. As part of this issue the TRG also briefly discussed the question of negative revenue but it did not go into detail and noted that negative revenue was not expected to be a pervasive issue.

59. Feedback summarised in paragraphs 48(b)–48(c) indicates there may be a lack of clarity on presentation of revenue amounts. Stakeholders did not express strong preference for either approach to presenting incentives or to recognising negative revenue. Instead, they asked the IASB to clarify the requirements to improve consistency in presentation.

60. Given the rising popularity of digital platforms that often offer large incentives to consumers, the materiality of amounts involved and the fact that there may be diversity in practice, we think it would be helpful to gather further evidence on prevalence of these matters and to ask for suggestions for resolving them. Therefore, the staff recommend including in the RFI a question on accounting for consideration payable to a customer.

Significant financing component

61. In developing the IFRS 15, the boards clarified that an entity should not update the discount rate for a change in circumstances because an entity should reflect in the measurement of the transaction price only the discount rate that is determined at contract inception. They also observed that it would be impractical for an entity to update the transaction price for changes in the assessment of the discount rate.[7] Given the requirement to use the discount rate at inception, the staff do not expect that there will be much diversity in practice in respect to the discount rate used.

62. The questions raised in paragraphs 49(b)–49(c) relate to narrow issues that are unlikely to affect many entities.

63. For the reasons in paragraphs 61–62, the staff recommend not including in the RFI a separate question on significant financing components.

[7] See paragraphs BC242–BC243 of the Basis for Conclusions on IFRS 15.

Other guidance on determining the transaction price

Non-cash consideration

64. As noted in paragraph 51(a), the FASB amended Topic 606 to clarify the date for measuring the fair value of non-cash consideration. The IASB decided not to specify the date to avoid a risk of potential unintended consequences because this issue has important interactions with other IFRS Accounting Standards including IFRS 2 *Share-based Payment* and IAS 21 *The Effects of Changes in Foreign Exchange Rates*. The IASB also noted that:
    - (a) discussions with some stakeholders highlighted that any practical effect of different measurement dates would arise in only limited circumstances; and
    - (b) paragraph 126 of IFRS 15 requires an entity to disclose information about the methods, inputs and assumptions used for measuring non-cash consideration.[8]

65. Phase 1 feedback does not indicate that the matter related to determining the date is widespread or that the lack of specific requirements in IFRS 15 has led to diversity that has significant effects. Therefore, the staff recommend not including in the RFI a specific question on accounting for non-cash consideration.

Sales-based taxes

66. The issue of accounting for sales taxes came up in TRG discussions and as a result the FASB decided to provide an accounting policy election to present all sales taxes on a net basis.

67. Paragraph BC188D of the Basis for Conclusions explains the IASB's reasons for deciding not to provide a similar accounting policy choice:
    - (a) it would maintain the comparability of revenue between entities operating under different tax regimes in different tax jurisdictions, as well as between entities operating in the same jurisdiction;

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[8] See paragraphs BC254B–BC254E of the Basis for Conclusions on IFRS 15.

(b) the IASB's previous revenue requirements contained requirements applicable to sales tax similar to those in IFRS 15, so it is not a new requirement for IFRS preparers; and

(c) providing the accounting policy choice would create an exception to the revenue recognition model that does not reflect the economics of the arrangement in cases in which a sales tax is a tax on the entity.

68. However, as mentioned in paragraph 51(b), phase 1 feedback indicates that there may be diversity in practice related to accounting for sales taxes. In our view, it would be helpful to gather further evidence on accounting for sales-based taxes to help the IASB assess the cause of any diversity, the prevalence of any diversity and the effects of any diversity. Therefore, the staff recommend including in the RFI a question on sales-based taxes. The RFI could also ask respondents for suggestions for guidance on assessing whether sales taxes are collected on behalf of a third party.

Step 4: Allocating the transaction price to the performance obligations in the contract

Background

69. The transaction price is allocated to each performance obligation in an amount to which the entity expects to be entitled in exchange for transferring the promised goods or services.

70. The allocation is based on the relative stand-alone selling prices (SSP) of each distinct good or service. If a SSP is not observable, an entity estimates it.

71. IFRS 15 provides guidance on methods that may be used for estimating a SSP—adjusted market assessment approach, expected cost plus a margin approach and

residual approach (the residual approach can be applied only if specified criteria are met).[9]

Overview of feedback

72. We received relatively little feedback on Step 4 in phase 1 outreach. Some preparers said that it was challenging to estimate stand-alone selling prices for some performance obligations, for example, if a new performance obligation has never been sold separately or has no or little cost. There were also some challenges with applying the residual approach for estimating a standalone selling price. However, in the preparers' view, practice has now developed.

73. A few stakeholders, mostly preparers from the telecommunications industry, said they still find the application of requirements on allocating the transaction price challenging and time-consuming. In addition, they expressed a view that some of the outcomes based on the requirements do not reflect the economics of their contracts. For example, in their view, price allocation between handsets and services does not reflect the economic substance because services end up with a low margin. These stakeholders suggested allowing more flexibility in applying the residual approach to allow entities to allocate the cost of the handset and a fixed margin to the handset and allocate the residual price to the services.

Staff analysis and recommendations

74. Phase 1 feedback does not indicate that there are pervasive matters with the requirements on allocating the transaction price to performance obligations. Therefore, the staff recommend not including in the RFI a specific question on the application of these requirements.

[9] See paragraphs 73–80 of IFRS 15.

Step 5: Recognising revenue when (or as) the entity satisfies a performance obligation

Background

75. An entity recognises revenue when (or as) goods or services are transferred to a customer—which is when the customer obtains control of that good or service.

76. Assessing when control of a good or service is transferred is a critical step in applying IFRS 15 and it is a change from the previous requirement to consider the risks and rewards of ownership.

77. To help preparers determine whether control transfers over time or at a point in time, paragraph 35 of IFRS 15 provides the criteria for revenue recognition over time:

    (a) the customer simultaneously receives and consumes the benefits provided by the entity's performance;

    (b) the entity's performance creates or enhances an asset that the customer controls as the asset is created or enhanced; or

    (c) the entity's performance does not create an asset with an alternative use to the entity and the entity has an enforceable right to payment.

78. For performance obligations satisfied over time, IFRS 15 provides guidance on selecting an appropriate measure of progress to determine how much revenue should be recognised as the performance obligation is satisfied.[10]

Overview of feedback

79. Some stakeholders of all types said that it was challenging to make an initial assessment of whether revenue should be recognised over time or at a point in time, in

[10] See paragraphs 39–45 of IFRS 15.

particular in the engineering, construction, automotive, equipment manufacturing, software development and gaming industries. Some of those stakeholders indicated that entities have largely overcome the initial challenges and practice has developed.

80. Some preparers said that internal management and users of financial statements considered that some changes to the timing of revenue recognition caused by transition to IFRS 15 did not reflect the economics of the transaction and found some of the changes counterintuitive, for example:

   (a) deferral of revenue related to research and development until the transfer of the final product even if an invoice for the R&D services is issued earlier;

   (b) moving from revenue recognition based on milestones to over time revenue recognition in businesses with long term contracts;

   (c) recognising revenue related to property development both over time and at a point in time depending on the terms of a contract; and

   (d) not recognising revenue upfront for a minimum guarantee payment in the media industry.

81. The main remaining challenges highlighted by stakeholders included:

   (a) applying the criteria for over time revenue recognition in paragraph 35 requires significant judgement. Stakeholders asked for more guidance on applying the criteria or illustrative examples for challenging fact patterns. Examples of challenging situations included:

      (i) considering breakage in accounting for pre-paid tariff plans in the telecommunications sector or in accounting for loyalty programmes;

      (ii) accounting for repurchase agreements, especially for fungible items such as cryptocurrencies and commodities; and

      (iii) determining when to recognise revenue for various offerings on gaming platforms.

(b) the requirement in paragraph 35(c) to assess whether an entity has an enforceable right to payment is seen as particularly challenging. An accounting firm said that despite the explanation in the Basis for Conclusions and the IC agenda decision *Revenue Recognition in a Real Estate Contract*, some preparers overlook the need to consider court judgements and suggested clarifying this in the Standard. Another stakeholder asked whether an entity needs to reassess the timing of revenue recognition if laws, regulations or court judgements change during the term of the contract.

(c) estimating the term for revenue recognition in some cases, for example, for:

(i) payments for goods that can only be used on a specific digital platform (estimating period of usage); or

(ii) non-refundable minimum payments.

82. A few stakeholders from Latin America, where local court practice prevents real estate developers from recognising revenue over time, suggested that the IASB consider providing more flexible criteria for over time revenue recognition.

83. We also heard a few suggestions related to measuring progress towards complete satisfaction of a performance obligation when revenue is recognised over time:

(a) an accounting firm shared their experience of auditors challenging entities' decisions to include the cost of uninstalled materials, which may be material, in the measure of progress when applying the input method. The stakeholder suggested defining or explaining the term 'uninstalled materials' to promote consistency in applying the requirements on recognising progress.

(b) a standard-setter asked for more guidance on selecting an appropriate method of measuring progress.

Staff analysis and recommendations

84. The previous revenue recognition requirements required an entity to assess the transfer of a good or service by considering the transfer of risks and rewards of

ownership. One of the reasons for the IASB's decision to require entities assess the transfer of a good or service by considering when the customer obtains control of that good or service was to provide a basis for more consistent decisions about when goods or services are transferred. This is because it can be difficult to judge whether an appropriate level of the risks and rewards of ownership of a good or service has been transferred to the customer if the entity retains some risks and rewards.[11]

85. The IASB expected some judgements, in particular those related to services and construction-type contracts, to be challenging. Indeed, phase 1 feedback indicates that many examples of challenging situations relate to complex arrangements involving services or intangible assets.

86. In our view, gathering further information about circumstances in which entities are unclear how to apply the requirements to determine the timing of revenue recognition will help the IASB assess whether the effects of the requirements are as expected. They will also help the IASB assess whether the requirements are capable of being applied consistently. Gathering more information on fact patterns that are causing challenges could help the IASB determine whether there is any diversity in practice for similar contracts, the prevalence of any diversity, and the effects of any diversity. The IASB could also ask stakeholders for suggestions for resolving the matter. Therefore, the staff recommend including in the RFI a question on determining the timing of revenue recognition, focusing on fact patterns in which the guidance is unclear or is applied inconsistently, in particular when applying the criteria for over time revenue recognition.

87. We do not suggest including a question related to measuring progress because:
    (a) we received little feedback on this matter;
    (b) the feedback on accounting for uninstalled materials suggests that the current requirements in IFRS 15 allow auditors to challenge accounting treatments they view as inappropriate; and
    (c) there are no suggestions of significant diversity in practice.

[11] See paragraph BC118 of the Basis for Conclusions on IFRS 15.