Staff paper

Agenda reference: 30B

IASB® meeting

Date	**March 2024**
Project	**Second Comprehensive Review of the *IFRS for SMEs®* Accounting Standard**
Topic	**Proposed revised Section 23 *Revenue from Contracts with Customers*—Additional and alternative simplifications**
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Introduction

1. The International Accounting Standards Board (IASB) proposed to revise Section 23 *Revenue* of the *IFRS for SMEs* Accounting Standard to align it with IFRS 15 *Revenue from Contracts with Customers* in the Exposure Draft *Third edition of the* IFRS for SMEs *Accounting Standard* (Exposure Draft). This paper discusses suggestions made by stakeholders about how to simplify the requirements proposed in the Exposure Draft.

2. In this paper, the term SMEs refers to entities that are eligible to apply the *IFRS for SMEs* Accounting Standard.

Purpose of the paper

3. The purpose of this paper is to ask the IASB:

   (a) to consider the suggestions made by stakeholders to simplify the requirements in the proposed revised Section 23 *Revenue from Contracts with Customers* of the Exposure Draft; and

   (b) to decide whether to change the proposed requirements.

Summary of staff recommendations

4. The staff recommend that the IASB:

   (a) not change the requirements proposed in the Exposure Draft for the simplifications suggested by stakeholders discussed in this paper; and

   (b) use the term 'collectability', instead of 'customer's credit risk', to express the requirement for an SME to estimate the recoverable amount of assets recognised from costs incurred to fulfil a contract.

Structure of the paper

5. This paper is structured as follows:

   (a) background (paragraphs 6–9);

   (b) suggested simplifications (paragraphs 10–12);

   (c) staff analysis of the suggested simplifications (paragraphs 13–19);

   (d) staff recommendations and question for the IASB (paragraph 20);

   (e) next steps (paragraph 21); and

   (f) Appendix—Simplifications suggested by stakeholders to the proposed requirements for revenue.

Background

6. The IASB applied its alignment principles when it developed the proposed revised Section 23.[1] In applying the principle of simplicity, the IASB proposed simplifications to the requirements in IFRS 15 to reduce the costs for SMEs of applying the Section.

[1] See Agenda Paper 30 *Cover paper* for this meeting and paragraphs BC29–BC32 of the Exposure Draft *Third edition of the* IFRS for SMEs *Accounting Standard* (Exposure Draft).

7. Paragraph BC16 of the Basis for Conclusions on the *IFRS for SMEs* Accounting Standard sets out five ways the requirements in full IFRS Accounting Standards can be simplified. They are:

   (a) omitting some topics;

   (b) permitting only the simplest option if an IFRS Accounting Standard permits options;

   (c) simplifying recognition and measurement requirements;

   (d) reducing disclosures; and

   (e) simplifying language.

8. In the Invitation to Comment in the Exposure Draft, comment letter respondents (respondents) were asked for suggestions of simplifications to the requirements in the proposed revised Section 23. A few respondents who commented on the Section suggested the IASB make additional or alternative simplifications.

9. Fieldwork was carried out on the proposed revised Section 23 with accounting practitioners involved in the preparation of SMEs' financial statements. Participants suggested ways of further simplifying the requirements in the Section.

Suggested simplifications

10. The appendix to this paper summarises the simplifications to the requirements in the proposed revised Section 23 suggested by respondents and fieldwork participants (stakeholders). It excludes suggestions to simplify the disclosure requirements, the presentation of the requirements and the language used in the Section. These suggestions will be covered in separate papers.

11. Apart from the suggestion to introduce an option for SMEs to recognise the costs of obtaining a contract as either an asset or expense, each suggestion was made by one or two stakeholders. Many of the suggestions were made by accounting bodies.

12. Some of the suggestions are similar to the requirements for revenue in the local accounting standards of particular jurisdictions.

Staff analysis

13. The appendix to this paper includes the staff analysis for each suggestion.

14. The IASB considered some of the suggestions at its previous meetings. The appendix refers to the papers that include the staff analysis of these suggestions. At its February meeting, the IASB tentatively decided to change the Exposure Draft for two of these suggestions:

    (a) to require an SME to account for an option that provides a material right to a customer as a separate promise, unless doing so involves undue cost or effort; and

    (b) to require an SME to recognise costs to obtain a contract as an expense when incurred.[2]

15. The staff recommend that the IASB not change the requirements proposed in the Exposure Draft for the other suggestions discussed in this paper, as explained in the appendix. The reasons for the recommendation vary and include:

    (a) the simplification would make the proposed requirements more difficult to apply;

    (b) the simplification would create additional complexity for SMEs;

    (c) the simplification would reduce comparability; and

    (d) the simplification would affect faithful representation, as well as moving the revised Section 23 away from the principles in IFRS 15.

[2] See IASB *Update* from the February 2024 IASB meeting.

16. Many of the suggestions would introduce accounting policy options in the revised Section 23. Introducing the suggested options would require the IASB to depart from its general approach of restricting accounting policy options in the *IFRS for SMEs* Accounting Standard. Options generally increase complexity and reduce comparability. The options in the Standard are also typically based on options provided in full IFRS Accounting Standards. For each suggested option, in addition to the reasons explained in the appendix, the staff think the possible cost savings resulting from the option would not justify the IASB departing from its general approach.

17. Some of the suggestions would allow SMEs to apply simpler accounting requirements based on materiality judgements in specific circumstances (for example, material to the contract). The proposed revised Section 2 *Concepts and Pervasive Principles* in the Exposure Draft describes materiality as a pervasive concept underlying SMEs' financial statements.[3] The proposed Section requires SMEs to make materiality judgements in the context of their financial statements as a whole. Requiring SMEs to make materiality judgements in different contexts risks confusing the concept of materiality. For this reason, the staff recommend not changing the proposed requirements for the suggestions based on materiality judgements, in additional to the reasons explained in the appendix.

Drafting change

18. Paragraph 23.113 of the Exposure Draft proposed requiring SMEs to adjust a contract's transaction price for the effect of the customer's credit risk when estimating the recoverable amount of assets recognised from the costs incurred to obtain or fulfil a contract. One respondent suggested removing the proposal to assess a customer's credit risk to avoid SMEs having to apply an expected credit loss (ECL) model for the impairment of financial assets.

[3] Paragraph 2.13 of the Exposure Draft.

19. The reference in paragraph 23.113 of the Exposure Draft to the effects of the customer's credit risk was not intended to result in SMEs applying an ECL model.[4] To make it clear that assessing customer credit risk is not the same as applying an ECL model, the staff recommend using the term 'collectability', instead of 'customer's credit risk', to express the requirement in the revised Section 23. For example, SMEs could be required to deduct from a contract's transaction price any consideration for which collection from the customer is not probable. The recommendation would help avoid SMEs associating the term 'customer's credit risk' with the application of an ECL model.

Staff recommendations and question for the IASB

20. The staff recommend that the IASB:

(a) not change the requirements proposed in the Exposure Draft for simplifications suggested by respondents discussed in this paper; and

(b) use the term 'collectability', instead of 'customer's credit risk', to express the requirement for an SME to estimate the recoverable amount of assets recognised from the costs incurred to fulfil[5] a contract.

Question for the IASB
Does the IASB agree to use the term 'collectability', instead of 'customer's credit risk', to express the requirement for an SME to estimate the recoverable amount of assets recognised from the costs incurred to fulfil a contract?

[4] In January 2024, the IASB tentatively decided to require SMEs that provide financing to customers as one of their primary businesses to apply an expected credit loss (ECL) model to measure the impairment of their financial assets. See IASB *Update* from the January 2024 IASB meeting.

[5] The respondent's suggestion relates to the requirement for subsequently measuring assets recognised from the costs incurred to obtain and fulfil a contract proposed in the Exposure Draft. In February 2024, the IASB tentatively decided to require SMEs to recognise the costs of obtaining a contract as an expense when incurred (see paragraph 14 of this paper). Consequently, SMEs will not recognise assets from the costs incurred to obtain a contract. The recommendation therefore relates to assets recognised from the costs incurred to fulfil a contract only.

Next steps

21. The staff will bring papers to the IASB on suggestions made by stakeholders:
    (a) to simplify the disclosure requirements in the proposed revised Section 23; and
    (b) to simplify the presentation of the requirements and language used in the proposed revised Section 23.

Appendix—Simplifications suggested by stakeholders to the proposed requirements for revenue

Topic	Stakeholders’ suggested simplification	Staff analysis
Step 1—Identify the contract(s) with a customer		
Combination of contracts	Introduce an option for SMEs to divide combined contracts into separate promises and recognise revenue for goods or services at an amount that corresponds with the amounts stipulated in the contact if: • doing so better represents the transaction with the customer; and • the value of the goods or services in the contract can be reasonably determined and does not differ materially from the stand-alone selling price of the goods or services. **Reason:** To avoid SMEs incurring undue cost or effort to combine contracts when accounting for each individual contract would not materially change revenue recognised.	The proposed requirements to combine contracts ensure the amount of consideration allocated to promises in the contracts faithfully depicts the consideration to which the SME expects to be entitled in exchange for the goods or services. Instances where separately accounting for contracts—that are required to be combined—would better represent the transaction are expected to be rare. The simplification would also require SMEs to assess whether separately accounting for contracts that are required to be combined would better represent the transaction with a customer. This assessment could require substantial judgement.
Contract modifications	Allow SMEs to account for contract modifications using any of the three approaches in paragraphs 23.14–23.15 of the Exposure Draft if the additional goods or services are immaterial to the contract. **Reason:** Comparability is unlikely to be significantly reduced if additional goods or services are immaterial to the contract.	The simplification would mean SMEs need not assess whether the effect of accounting for contract modifications—that are immaterial at a contract level—is material to the financial statements as a whole. However, this assessment is not considered unduly burdensome because: • SMEs are generally expected to have fewer contracts with customers compared with entities applying IFRS 15; and • contract modifications that relate to goods or services that are immaterial often relate to contracts with similar goods or services that are modified regularly. In such instances, SMEs might assess materiality by considering the modifications on an aggregated basis.

Topic	Stakeholders’ suggested simplification	Staff analysis
Contract modifications	Express the requirements about how to account for a contract modification in relation to whether the modification results in the customer receiving something different from, or similar to, the goods or services promised in the contract. **Reason:** To make the requirements easier to understand.	The simplification would replace the term ‘distinct’ with the term ‘different’. Under the proposed requirements, goods and services that are distinct might not be different. Therefore, the suggested simplification could result in SMEs accounting for contract modifications in a way that does not faithfully depict the SMEs’ rights and obligations arising from the modified contract. The revised Section 23 will include the notion of distinct when identifying promises in a contract. Therefore, the benefits of introducing an alternative concept for contract modifications would be limited.
Contract modifications	Express the requirements about how to account for a contract modification as a change in accounting estimate. **Reason:** To make the requirements easier to understand.	Contract modifications arise from changes to the contract and, thus, are not changes in accounting estimates. Requiring SMEs to account for contract modifications as if they were changes in accounting estimates would be inconsistent with Section 10 *Accounting Policies, Estimates and Errors* of the *IFRS for SMEs* Accounting Standard. If SMEs account for contract modifications as if they were changes in accounting estimates, they would need to determine the effect of the change. Section 10 includes no guidance to help SMEs do so.

Topic	Stakeholders' suggested simplification	Staff analysis
Step 2—Identify the promises in the contract		
Series of distinct goods or services	Introduce an option for SMEs to divide into separate promises a promise to transfer a series of distinct goods or services that are substantially the same, and that have the same pattern of transfer to the customers. The promise would be divided based on units of time (for example, each month, quarter or year). **Reason:** To allow revenue recognised for a multi-year contract to be aligned with how the contract is priced.	The IASB considered a similar simplification when it developed the Exposure Draft. The IASB rejected the simplification because the proposed requirements for allocating variable consideration would achieve an outcome similar to the simplification.[6] If the price of a multi-year contract varies in such a way that it depicts the amount of consideration that the SME expects to be entitled to for transferring the goods or services, the revenue recognised for the contract would be aligned with how the contract is priced. The simplification would accommodate contracts for which the promised consideration changes for reasons other than because the transaction price includes a variable amount. However, doing so would undermine the principles in IFRS 15 and make the revised Section 23 more complex.
Distinct goods or services	Do not require SMEs to assess whether goods or services promised to a customer are distinct if they are immaterial within the context of the contract. **Reason:** Comparability is unlikely to be significantly reduced if the additional goods or services are immaterial within the context of the contract.	The simplification would mean SMEs need not assess whether the effect of accounting for goods or services—that are immaterial at a contract level—is material to the financial statements as a whole. SMEs must assess materiality when determining the unit of account in other areas of the *IFRS for SMEs* Accounting Standard. The Standard does not exempt SMEs from having to aggregate transaction that are individually immaterial and assess if they are material to the financial statements as a whole.

[6] Paragraphs 71–75 of Agenda Paper 30B *Towards an exposure draft—Additional simplifications to IFRS 15* Revenue from Contracts with Customers of the June 2022 IASB meeting.

Topic	Stakeholders' suggested simplification	Staff analysis
Distinct goods or services	Introduce an option for SMEs to account for shipping and delivery activities that occur after a customer has obtained control of a good as an activity to fulfil the promise to transfer the good, instead of assessing whether the activities are distinct. **Reason:** To reduce costs. In these instances, the cost of recognising shipping and delivery activities as separate promises is likely to outweigh the benefit of the information.	The option would reduce comparability. In particular, the option would make it difficult for users to compare revenue reported by SMEs with significant shipping operations that choose to account for shipping and delivery activities differently. The option would apply only to shipping and delivery activities. SMEs might provide other services after a customer has obtained control of a good (for example, storage or custodial services). Consequently, the option would be inconsistent with the general requirements for assessing whether other activities provide the customer with a distinct good or service.
Warranties	Allow SMEs to disclose 'free' warranties provided to customers as contingent liabilities, instead of accounting for them in accordance with Section 21 *Provisions and Contingencies* or the revised Section 23 of the *IFRS for SMEs* Accounting Standard. **Reason:** None given.	The simplification would mean SMEs need not assess whether a warranty is distinct. The exemption would apply only if the warranty were provided for 'free'. This would be inconsistent with the general requirements for assessing whether a service is distinct, which apply to: • warranties for which customers are charged; and • other services provided for 'free' (for example, installation or maintenance services).
Customer options for additional goods or services	Introduce criteria to identify when an SME accounts for a customer option as a separate promise. **Reason:** To make it easier to make materiality judgements about customer options.	Feedback from fieldwork participants indicates that SMEs would find it difficult to make materiality judgements about customer options because they do not capture information about those options. Introducing the suggested criteria would not overcome this difficulty.
Customer options for additional goods or services	Require SMEs to account for an option that provides a material right to a customer as a separate promise, unless doing so involves undue cost or effort. **Reason:** None given.	The IASB decided to change the proposed requirements for this suggestion. See paragraphs 24–44 of Agenda Paper 30C *Proposed revised Section 23* Revenue from Contracts with Customers—*Redeliberation topics* of the February 2024 IASB meeting.

Topic	Stakeholders' suggested simplification	Staff analysis
Step 3—Determine the transaction price		
Variable consideration	Require SMEs to determine the amount of variable consideration based on the actual amount of consideration received instead of an estimate. **Reason:** To avoid having to estimate variable consideration. The consideration would be expected to be received by the time the SME's financial statements are authorised for issue.	The IASB decided not to change the proposed requirements for this suggestion. See paragraphs 87–104 of Agenda Paper 30C *Proposed revised Section 23* Revenue from Contracts with Customers—*Redeliberation topics* of the February 2024 IASB meeting.
Refund liabilities	Require SMEs to recognise a refund liability only if the terms for a refund are in addition to those required by law (that is, a customer's right to a refund is in addition to the minimum statutory right to a refund). **Reason:** None given.	A customer's right to a refund may arise from contractual or legal rights. However, the right to a refund is similar, regardless of how it arises. Consequently, the simplification would mean an SME would account for similar rights differently.
Time value of money	Do not require SMEs to adjust for the time value of money when payment is expected to be deferred by one year or less (that is, make the exemption in paragraph 23.59 of the Exposure Draft mandatory). **Reason:** To reduce the judgement needed to apply the revised Section 23.	Instances may arise when adjusting the promised amount of consideration for the effects of the time value of money in short-term contracts is material (for example, contracts with high implicit interest rates—common in jurisdictions with high (or hyper) inflation). Adjusting the promised amount of consideration for the time value of money in these instances, as permitted in the proposed revised Section 23, would more faithfully represent the transaction. The simplification would therefore prevent SMEs from providing more useful information in such instances.

Topic	Stakeholders’ suggested simplification	Staff analysis
Non-cash consideration	Present the exemption from measuring the fair value of non-cash consideration in paragraph 23.60 of the Exposure Draftas an undue cost or effort exemption. **Reason:** To make the requirements easier to understand. The *IFRS for SMEs* Accounting Standard typically requires SMEs to measure items at fair value only if a reliable measure of fair value is available without undue cost or effort.	Under the proposals, if an SME cannot *reasonably estimate* the fair value of non-cash consideration, the consideration would be measured indirectly by reference to the stand-alone selling price of the goods or services promised to the customer in exchange for the consideration (that is, the SME would apply the exemption). This is aligned with the requirements for measuring non-cash consideration in IFRS 15. The simplification would require SMEs to assess the costs and benefits of measuring the fair value of the non-cash consideration in order to apply the exemption. Consequently, SMEs would have to meet more stringent requirements to apply the exemption compared with entities applying IFRS 15.
Step 4—Allocate the transaction price to the promises in the contract		
Allocation based on stand-alone selling prices	Do not require SMEs to allocate the transaction price to the promises in a contract in specific instances. **Reason:** None given.	The IASB decided not to change the proposed requirements for this suggestion. See paragraphs 115–125 of Agenda Paper 30C *Proposed revised Section 23* Revenue from Contracts with Customers—*Redeliberation topics* of the February 2024 IASB meeting.

Topic	Stakeholders' suggested simplification	Staff analysis
Estimating stand-alone selling prices	Allow SMEs to use the residual approach to estimate the stand-alone selling price of goods or services that are immaterial to other goods or services in the contract. **Reason:** Comparability is unlikely to be significantly reduced if the additional goods or services are immaterial to other goods or services in the contract.	Guidance proposed in the Exposure Draft specifies when SMEs may use the residual approach to estimate the stand-alone selling price of goods or services. At its February 2024 meeting, the IASB decided to include guidance on methods for estimating stand-alone selling prices in separate educational material instead of in the revised Section 23.[7] Guidance in the educational material is non-mandatory. As the revised Section 23 will not specify when an SME can use the residual approach, the simplification is unnecessary.
Estimating stand-alone selling prices	Allow SMEs to allocate the transaction price to options that provide material rights to customers based on the future selling price of the additional goods or services provided by the option, rather than the stand-alone selling price of the option. **Reason:** None given.	The proposed requirements for estimating the stand-alone selling price for customer options require the price to reflect: • any discount the customer could receive without exercising the option; and • the likelihood that the option will be exercised. Allocating the transaction price to an option based on the future selling price of the additional goods or services would mean the amount of revenue recognised for the option would not be adjusted for the above factors and would be overstated. Also, if an SME ignores these factors when estimating the stand-alone selling price, the SME might separately account for options in instances in which the resulting information is immaterial.

[7] See IASB *Update* from the February 2024 IASB meeting.

Topic	Stakeholders' suggested simplification	Staff analysis
Step 5—Recognise revenue when (or as) the entity satisfies a promise		
Promises satisfied over time	Allow SMEs to treat promises satisfied over time as promises satisfied at a point in time if they are made up of a large number of goods or services that are: • transferred over a short period of time; and • of a low value. **Reason:** None given.	The simplification would benefit SMEs if the transfer of goods or services is over a short period of time but spans reporting periods. Consequently, the simplification is expected to benefit SMEs in a limited number of instances. The simplification would also require SMEs to assess whether: • a period of time is 'short'; and • a good or service is low value. Both assessments could be made differently by SMEs in similar circumstances. This would reduce the comparability of revenue information among SMEs.
Promises satisfied at a point in time	Allow SMEs to recognise revenue on the date the asset is shipped, instead of the date on which the customer obtains control of the asset, if: • the good is sold domestically; and • the period of time from when the good is shipped until the customer obtains control is typical for the jurisdiction. **Reason:** Comparability is unlikely to be significantly reduced if revenue is recognised on the date a good is shipped, instead of the date on which the customer obtains control of the good.	The simplification is based on the assumption that, for goods sold domestically, the period of time—from when the good is shipped until the customer obtains control of the good—is short. However, that assumption may not be true for all jurisdictions, where domestic shipping times could be long. The simplification also requires an SME to assess whether the period of time from when a good is shipped until the customer obtains control of the good is typical for the jurisdiction. The assessment therefore requires an SME to identify when a customer obtains control in a typical contract, which could be made differently by SMEs in similar circumstances.

Topic	Stakeholders' suggested simplification	Staff analysis
Contract costs		
Cost to obtain a contract	Require SMEs to recognise costs to obtain a contract as an expense when incurred. **Reason:** To reduce costs. Generally, the cost of recognising costs to obtain a contract as an asset is likely to outweigh the benefit of the information.	The IASB decided to change the proposed requirements for this suggestion. See paragraphs 45–64 of Agenda Paper 30C *Proposed revised Section 23 Revenue from Contracts with Customers—Redeliberation topics* of the February 2024 IASB meeting.
Cost to obtain a contract	Introduce an option to recognise the costs to obtain a contract as either an asset or an expense. **Reason:** To reduce costs and the judgement needed to apply the revised Section 23. Applying the proposed undue cost or effort exemption involves significant judgement and requires SMEs to identify the costs to obtain a contract. Identifying the costs to obtain a contract can be the most difficult part of accounting for the costs.	The IASB decided not to change the proposed requirements for this suggestion. See paragraphs 45–64 of Agenda Paper 30C *Proposed revised Section 23 Revenue from Contracts with Customers—Redeliberation topics* of the February 2024 IASB meeting.
Costs of fulfilling a contract	Introduce an option to recognise the costs of fulfilling a contract as an expense when incurred for short contracts (those for which the amortisation period for the asset would have been one year or less). **Reason:** None given.	The simplification is similar to the expedient in paragraph 23.105 of the Exposure Draft for costs to obtain a contract. However, the costs of fulfilling a contract are typically much larger than the costs to obtain a contract. The simplification would result in SMEs recognising different profit margins for similar contracts depending on whether the expedient has been applied. Because costs to fulfil a contract can be significant, the suggested simplification would make it difficult for users to understand and compare the profit margins of SMEs that choose to account for costs to fulfil a contract differently.

Topic	Stakeholders' suggested simplification	Staff analysis
Measurement after recognition	When applying paragraph 23.112(a) of the Exposure Draft, do not require an SME to adjust the transaction price for the effects of a customer's credit risk. **Reason:** To remove what the stakeholder views as inappropriate requirements. Most SMEs are expected to apply the incurred loss model for the impairment of financial assets.	The simplification would remove the requirement for SMEs to assess customer credit risk. By not assessing customer credit risk, assets recognised from the costs to obtain or fulfil a contract could be overstated. The simplification aims to prevent SMEs from having to apply an expected credit loss model for the impairment of financial assets. This is not a requirement of paragraph 23.113 of the Exposure Draft. The staff recommend changing how the requirement is drafted to make this clear (see paragraphs 18–19 of this paper)
Consequential amendments		
Scope of Section 13 *Inventories*	Remove materials and supplies to be consumed in the rendering of services from the scope of Section 13 *Inventories* of the *IFRS for SMEs* Accounting Standard. **Reason:** To simplify the requirements. Accounting for these costs is covered by the proposed requirements for costs of fulfilling a contract.	The proposed requirements for recognising costs to fulfil a contract as an asset are more general compared with the requirements in Section 13 about costs included in inventories. Therefore, the simplification would make it more difficult to determine whether the costs of rendering services can be recognised as an asset. Also, because the criteria are more general, SMEs may apply them inconsistently and recognise similar costs differently. This would reduce the comparability of profit margins among SMEs.
Application of the model		
Screening test	Introduce a screening test for SMEs with simple contracts that means they need not make a detailed assessment of the requirements that cover each step of the revenue recognition model. **Reason:** To make the requirements easier to apply.	The IASB decided not to change the proposed requirements for this suggestion. See paragraphs 49–50 of Agenda Paper 30A *Proposed revised Section 23 Revenue from Contracts with Customers* of the October 2023 IASB meeting.