

28 October 2015

International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH
United Kingdom
Email: CommentLetters@ifrs.org

Dear Sir/Madam

SAICA SUBMISSION ON ED/2015/6 – CLARIFICATIONS TO IFRS 15

In response to your request for comments on ED/2015/6 – *Clarifications to IFRS 15*, attached is the comment letter prepared by the Accounting Practices Committee (APC) of The South African Institute of Chartered Accountants (SAICA). This comment letter results from deliberations of the APC, which comprises members from reporting organisations, regulators, investment analysts, auditors, IFRS specialists and academics.

We thank you for the opportunity to provide comments on this document.

Please do not hesitate to contact us should you wish to discuss any of our comments.

Yours faithfully,

Prof Danie Coetsee
Chairman of the Accounting
Practices Committee

Bongeka Nodada
Project Director – Financial
Reporting Standards

SAICA SUBMISSION ON ED/2015/6 – CLARIFICATIONS TO IFRS 15 – REVENUE FROM CONTRACTS WITH CUSTOMERS

GENERAL COMMENTS

We welcome the efforts by the International Accounting Standards Board (IASB or Board) to provide additional clarifications and transition reliefs when entities adopt the new revenue Standard.

We support the convergence of IFRS 15 – *Revenue from Contracts with Customers* with Accounting Standards Codification (ASC) 606, and believe that the wording in both Standards should be aligned. Should this not be case, there could be unintended consequences in that both Standards could be interpreted differently in practice. We also request that the IASB should acknowledge that the use of different wording in both Standards could produce different outcomes and therefore result in Standards that are no longer converged whilst also indicating why convergence on the topic is not achieved. Our comments to individual questions should be analysed in the context of these general comments.

We also believe that it is very difficult to raise implementation issues until the Standard is fully implemented.

SPECIFIC COMMENTS

Question 1—Identifying performance obligations

IFRS 15 requires an entity to assess the goods or services promised in a contract to identify the performance obligations in that contract. An entity is required to identify performance obligations on the basis of promised goods or services that are distinct.

To clarify the application of the concept of ‘distinct’, the IASB is proposing to amend the Illustrative Examples accompanying IFRS 15. In order to achieve the same objective of clarifying when promised goods or services are distinct, the FASB has proposed to clarify the requirements of the new revenue Standard and add illustrations regarding the identification of performance obligations. The FASB’s proposals include amendments relating to promised goods or services that are immaterial in the context of a contract, and an accounting policy election relating to shipping and handling activities that the IASB is not proposing to address. The reasons for the IASB’s decisions are explained in paragraphs BC7–BC25.

Do you agree with the proposed amendments to the Illustrative Examples accompanying IFRS 15 relating to identifying performance obligations? Why or why not? If not, what alternative clarification, if any, would you propose and why?

We do not agree with the IASB’s approach to clarify the application of the concept of ‘distinct’ by amending the Illustrative Examples accompanying IFRS 15. We believe that the clarifications in the Illustrative Examples are not effective, and therefore we recommend that the IASB follows the FASB approach and amend the wording on the Standard to clarify the requirements on identifying performance obligations and include the examples to ensure that the requirements between the two Standards remained aligned. Also refer to our general comments raised earlier in this letter.

We agree with the IASB’s decision not to include the accounting policy election relating to the shipping and handling activities as worldwide shipping and handling could be material.

SAICA SUBMISSION ON ED/2015/6 – CLARIFICATIONS TO IFRS 15 – REVENUE FROM CONTRACTS WITH CUSTOMERS

We also believe that the shipping and handling activities should be determined on a contract by contract basis because in some contracts the shipping and handling activities might be a significant component that is contracted for whereas to other contracts it might not be. This will also depend on the contract's stipulated Incoterms, such as (FOB) and Delivered at Place DAP. Under FOB control of the delivered goods transfer to the customer when loaded, thereby implying that shipping might be a separate performance obligation as it relates to a promise fulfilled after control of the goods is transferred. Under DAP the seller retains responsibility for the sold goods until the customer unloads the goods, in which case delivery is unlikely to be a separate performance obligation as the performance obligation could be to provide goods at a specified location. Including such examples in IFRS 15's Implementation Guidance would be beneficial.

However, some of the constituents believe that the Board should follow the FASB approach and include the proposed amendment to the accounting policy election relating to shipping and handling activities to maintain convergence. This inconsistency is especially concerning for foreign private issuers.

We believe that the Board should specify the practical expedient of not identifying promised goods or services that are considered to be immaterial. The Board should also provide guidance in assessing materiality in the context of IFRS 15, i.e. contract level or overall level.

Question 2—Principal versus agent considerations

When another party is involved in providing goods or services to a customer, IFRS 15 requires an entity to determine whether it is the principal in the transaction or the agent. To do so, an entity assesses whether it controls the specified goods or services before they are transferred to the customer.

To clarify the application of the control principle, the IASB is proposing to amend paragraphs B34–B38 of IFRS 15, amend Examples 45–48 accompanying IFRS 15 and add Examples 46A and 48A.

The FASB has reached the same decisions as the IASB regarding the application of the control principle when assessing whether an entity is a principal or an agent, and is expected to propose amendments to Topic 606 that are the same as (or similar to) those included in this Exposure Draft in this respect.

The reasons for the Boards' decisions are explained in paragraphs BC26–BC56.

Do you agree with the proposed amendments to IFRS 15 regarding principal versus agent considerations? In particular, do you agree that the proposed amendments to each of the indicators in paragraph B37 are helpful and do not raise new implementation questions? Why or why not? If not, what alternative clarification, if any, would you propose and why?

We agree with the proposed amendments to IFRS 15 regarding principal versus agent considerations. The proposed amendments are easier to read and are a good improvement.

SAICA SUBMISSION ON ED/2015/6 – CLARIFICATIONS TO IFRS 15 – *REVENUE FROM CONTRACTS WITH CUSTOMERS*

We suggest that the IASB should add the following indicator in paragraph B37 as it would work better with the indicators that an entity can use to assess the control of the specified service:

- To supply a choice of a supplier. For example intermediary agent has a choice to choose its own supplier for the services before the services reaches the customer. Therefore the intermediary agent is directing the supplier to provide goods or services to the customer and would have control.

We also suggest that the guidance in paragraph BC55(b)(i) and (ii) be included in the Standard, rather than in the Basis for Conclusions to make it more authoritative.

We acknowledge that the control principle sometimes causes problems when assessing a principal or agent relationship:

- For example, an international company directs the South African company to perform certain services for them and effectively the international company would always be the principal in this relationship and the South African company would be the agent. However if the control principle is being used to determine the principal and agent relationship, the South African company would be the principal as it controls the specified services before they are transferred to the customer of the international company. An example of this is where a local data provider provides for the streaming of recorded media for the consumption on its customers' handsets. The question is if the data provider controls the recorded media the moment before transferring it to the customer as they can interrupt or completely stop the streaming and the recorded media is contained on their server before transmitting.
- Applying a control model might have unintended consequences for certain financial institutions. It is not clear where the financial institution obtains control momentarily before the good is transferred to the customer. These institutions see themselves as agents under these circumstances, but this could result in a principal relationship.

We also have a concern that paragraph B35A(c) reads as an application rule of an indicator in paragraph 35A(b) rather than as a principle.

Some of the Illustrative Examples do not take into account the assessment of the indicators in paragraph B37 to determine whether an entity is acting as an agent or a principal. The current wording refers to control and the indicators are treated as an afterthought. We are therefore concerned that some entities will simply ignore the indicators. We further have a concern regarding the weighting that should be applied to indicators used to determine whether an entity is acting as an agent or a principal as some of the entities would apply professional judgement in determining whether an entity is acting as an agent or a principal. We recommend that all the Illustrative Examples include both the assessment of the control principle and the indicators in paragraph B37, thereby indicating how the control principle is applied under certain circumstances.

SAICA SUBMISSION ON ED/2015/6 – CLARIFICATIONS TO IFRS 15 – REVENUE FROM CONTRACTS WITH CUSTOMERS

Question 3—Licensing

When an entity grants a licence to a customer that is distinct from other promised goods or services, IFRS 15 requires the entity to determine whether the licence transfers to a customer either at a point in time (providing the right to use the entity’s intellectual property) or over time (providing the right to access the entity’s intellectual property). That determination largely depends on whether the contract requires, or the customer reasonably expects, the entity to undertake activities that significantly affect the intellectual property to which the customer has rights. IFRS 15 also includes requirements relating to sales-based or usage-based royalties promised in exchange for a licence (the royalties constraint).

To clarify when an entity’s activities significantly affect the intellectual property to which the customer has rights, the IASB is proposing to add paragraph B59A and delete paragraph B57 of IFRS 15, and amend Examples 54 and 56–61 accompanying IFRS 15. The IASB is also proposing to add paragraphs B63A and B63B to clarify the application of the royalties constraint. The reasons for the IASB’s decisions are explained in paragraphs BC57–BC86.

The FASB has proposed more extensive amendments to the licensing guidance and the accompanying Illustrations, including proposing an alternative approach for determining the nature of an entity’s promise in granting a licence.

Do you agree with the proposed amendments to IFRS 15 regarding licensing? Why or why not? If not, what alternative clarification, if any, would you propose and why? or why not? If not, what alternative clarification, if any, would you propose and why?

We believe that the approach proposed by the IASB regarding licensing is better as it is principles-based. The FASB’s approach has its own merits and disadvantages.

We believe that the IASB’s guidance is consistent with the principle in the Standard whereas the FASB’s guidance is easier to apply. However, we acknowledge that both the proposed licensing approaches are different and the outcomes will not be the same. Therefore in order to achieve convergence we recommend that both the FASB and the IASB should have the same wording/amendments to both Standards. Alternatively the IASB Basis for Conclusions should indicate how the FASB’s decision tree meets or contradicts the IASB principles. Also refer to our general comments raised earlier in this letter.

We have concerns with Example 11 Case E dealing with consumables. The example indicates that if the consumables are readily available from the supplier (even if the supplier is the only one that produces it) the consumables would be distinct from the equipment. If this rationale is applied to a situation where a customer can only use the company’s set-top box to stream programmes, it would result in two performance obligations. This view is contrary to how we understand such transactions should be accounted for, i.e. as a single performance obligation.

BC 81 states that restrictions do not affect the number of performance obligations. However, in the current FASB example, the restrictions did have an effect on the number of performance obligations. The question was therefore raised if this should be a rule or should we leave it to facts and circumstances.

The proposed change to 606-10-55-64 could be good application guidance and should be included in the Basis for Conclusions or to IFRS 15.B62: “A restriction defines the scope of a

SAICA SUBMISSION ON ED/2015/6 – CLARIFICATIONS TO IFRS 15 – REVENUE FROM CONTRACTS WITH CUSTOMERS

customer's right to use or right to access intellectual property. Therefore, an entity assesses whether a contractual provision defines the scope of the customer's right to use or right to access the intellectual property to determine whether that provision is a restriction."

Question 4—Practical expedients on transition

The IASB is proposing the following two additional practical expedients on transition to IFRS 15:

- (a) to permit an entity to use hindsight in (i) identifying the satisfied and unsatisfied performance obligations in a contract that has been modified before the beginning of the earliest period presented; and (ii) determining the transaction price.*
- (b) to permit an entity electing to use the full retrospective method not to apply IFRS 15 retrospectively to completed contracts (as defined in paragraph C2) at the beginning of the earliest period presented.*

The reasons for the IASB's decisions are explained in paragraphs BC109–BC115. The FASB is also expected to propose a practical expedient on transition for modified contracts. Do you agree with the proposed amendments to the transition requirements of IFRS 15? Why or why not? If not, what alternative, if any, would you propose and why?

We do not oppose this practical expedient. Our concern is with regards to what constitutes a completed contract as the term is not adequately defined. It is not clear if 'complete' refers to revenue recognition or delivery of the promised goods or services. We would appreciate additional clarifications in this regard.

We also believe that this is an area that the IASB and FASB should converge as an entity reporting under IFRS and US GAAP could reach a different answer under IFRS and US GAAP if convergence is not achieved.

Question 5—Other topics

The FASB is expected to propose amendments to the new revenue Standard with respect to collectability, measuring non-cash consideration and the presentation of sales taxes. The IASB decided not to propose amendments to IFRS 15 with respect to those topics. The reasons for the IASB's decisions are explained in paragraphs BC87–BC108.

Do you agree that amendments to IFRS 15 are not required on those topics? Why or why not? If not, what amendment would you propose and why? If you would propose to amend IFRS 15, please provide information to explain why the requirements of IFRS 15 are not clear.

We agree that amendments are not required to IFRS 15 on collectability as there is sufficient guidance on the Standard and the Basis for Conclusions which should get you to the same answer.

We believe that the reason why the IASB is not proposing an amendment on measuring non-cash consideration is because of what the IFRS Interpretations Committee has proposed recently on the draft IFRIC Interpretation on Foreign currency Transactions and Advance Consideration. This is different to the amendments we anticipate the FASB to propose. We suggest that the IASB should include in the Basis for Conclusions the discussion on the draft

SAICA SUBMISSION ON ED/2015/6 – CLARIFICATIONS TO IFRS 15 – *REVENUE FROM CONTRACTS WITH CUSTOMERS*

IFRIC Interpretation on Foreign currency Transactions and Advance Consideration relating to the date of fair value measurement for non-cash consideration.

We agree that amendments are not required to IFRS 15 on presentation of sales tax as this is not a practical expedient but it is a practical exception. The IASB should acknowledge that treatment of sales taxes between entities can differ due to jurisdictional requirements and rather provide guidance in this regard.

Not making these changes could result in a failure to achieve convergence between IFRS and US GAAP. We do however not advocate blindly following the FASB's proposed amendments as this may contradict the principles-based approach used in IFRS. Should this approach be followed, the Basis for Conclusions should then acknowledge that there is divergence between the two revenue Standards. Also refer to our general comments raised earlier in this letter.

#534383