MAZARS

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

26 October 2010

Dear Sir/Madam,

Re : Revenue from contracts with customers

Mazars welcomes the opportunity to comment on the Exposure Draft (ED) *Revenue from Contracts with Customers.*

Although we understand the Boards' objective of convergence, we believe that the current revenue recognition models proposed in IAS 11 and IAS 18 work well and provide useful information to users. We are not convinced that the model proposed in the ED is an improvement to the existing standards.

We acknowledge that some of the inconsistencies and weaknesses pointed out by respondents in their answers to the Discussion Paper have been reduced. But we believe the proposed model still needs to be improved in order to be applied consistently and to be decision-useful to users, especially when it relates to construction contracts and rendering of services.

Our detailed comments can be summarized as follows:

- In our view, the definition of control still needs to be clarified in order to be applied consistently. Indeed, some of the indicators proposed in the ED do not seem to be workable when applied to construction contracts or service arrangements. We believe that financial statements are more decision-useful to users if revenue associated with construction contracts are recognised continuously over the contract period. We think the ED should clarify that if an entity meets the "customer specific" indicator, the goods or services are transferred to the customer continuously.

- We do not think that an entity should systematically take into account what other entities sell in order to identify performance obligations. Rather, we believe the entity should consider its own business model. In complex contracts in which the tasks are highly interrelated, we believe that the entity should generally identify only one performance obligation being the construction contract as a whole, even if each task in the contract could be sold separately by other entities.

- We think the "performance obligation" notion should have an impact solely on the timing of revenue recognition. Thus, we believe that an entity should recognise a

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liability only if a contract as a whole is or becomes onerous. Likewise, in respect of an amendment to an existing contract, we believe that changes in the transaction price should be allocated to the contract as a whole (and thus to all performance obligations in the contract). Both these analyses take into consideration the fact that construction or service contracts and their amendments are usually negotiated globally without considering the margin expected on each performance obligation.

- We do not agree that an entity should recognise revenue on the basis of the expected value method described in the ED. Rather, we would favour an approach in which revenue is recognised only when it is highly probable, in line with the current model.

- We agree that the transaction price should reflect the customers' credit risk but do not believe that the effects of the customers' credit risk should affect the revenue line, rather be considered as an expense shown within the operational profit.

- We do not agree with the proposals in the ED related to legal warranties. We do not understand their rationale and think that the proposed accounting does not work well when the warranty covers defects of products' components. We believe all the warranties should be accounted for as separate performance obligations. Should the Boards consider that legal warranties are not separate performance obligations, we believe the entity should account for a provision in accordance with current IAS 37.

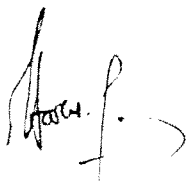
- We believe the disclosure requirements are excessive and burdensome.

- On the principle, we agree that the final standard should be applied retrospectively. However, we believe this retrospective application may be impracticable (as defined in IAS 8) for entities that conclude very long term contracts. We would favour some transitional provisions to avoid complexity.

We would be pleased to discuss our comments with you and remain at your disposal should you require further clarification or additional information.

Yours sincerely

Michel Barbet-Massin



Head of Financial Reporting Technical support

Question 1 — Paragraphs 12–19 propose a principle (price interdependence) to help an entity determine whether:

(a) **to combine two or more contracts and account for them as a single contract;**

(b) **to segment a single contract and account for it as two or more contracts; and**

(c) **to account for a contract modification as a separate contract or as part of the original contract.**

Do you agree with that principle? If not, what principle would you recommend, and why, for determining whether (a) to combine or segment contracts and (b) to account for a contract modification as a separate contract?

We overall agree with the proposed guidance on combining and segmenting contracts. However, we believe the Boards should explain the rationale used in example 2 (scenario 2).

In respect of an amendment to an existing contract, we believe that changes in the transaction price should be allocated to the contract as a whole (and thus to all performance obligations in the contract). Indeed, we think the "performance obligation" notion should have an impact solely on the timing of revenue recognition.

Question 2 — The boards propose that an entity should identify the performance obligations to be accounted for separately on the basis of whether the promised good or service is distinct. Paragraph 23 proposes a principle for determining when a good or service is distinct. Do you agree with that principle? If not, what principle would you specify for identifying separate performance obligations and why?

We do not think that an entity should systematically take into account what other entities sell in order to identify performance obligations. Rather, we believe the entity should consider its own business model.

As mentioned in the ED, we believe that in complex contracts (such as construction contracts as defined in IAS 11), some or all of the tasks are "highly interrelated because the entity provides a significant service by coordinating those tasks and covering the risk that those tasks do not combine". In that case, we believe that the entity should generally identify only one performance obligation being the construction contract as a whole, even if each task in the contract could be sold separately by other entities.

In example 11, in our opinion, the design phase should not be identified as a separate performance obligation if the entity's business model is not to sell this task separately and if the design phase and the construction phase are highly interrelated (even if the design phase could be sold separately by other entities). The same rationale could be used for the site preparation and site finishing, as these tasks are not sold separately by the entity and seem to be highly interrelated.

Moreover, when the tasks are highly interrelated, we do not think there is any benefit for users if the proposals of the ED lead to the disaggregation of a construction contract in separate performance obligations. Indeed, in our view, users are more interested in the total contract profit margin than in revenue and profit margin of an individual good or service in the contract.

When it relates to post contract services such as maintenance, additional warranties or options for additional goods or services that provide a material right to the customers, we agree that they should be identified as separate performance obligations. Once again, this is in line with our view that an entity should recognise performance obligations based on its business model.

Question 3 — Do you think that the proposed guidance in paragraphs 25–30 and related application guidance is sufficient for determining when control of a promised good or service has been transferred to a customer? If not, why? What additional guidance would you propose and why?

In the ED, the Boards propose that revenue should be recognised only when an entity transfers a promised good or service to a customer, thereby satisfying a performance obligation in the contract.

The Boards decided that an entity should assess whether a transfer of an asset has occurred by considering whether the customer obtains control. The Boards have given a definition of control and developed some indicators to determine when control has been transferred to the customer.

Respondents to the DP were concerned about the application of the control guidance to contracts in the construction industry. They thought the proposals could result in revenue recognition for construction contracts only upon transfer of legal title or physical possession of the asset, which often happens upon contract completion.

We understand the Boards do not intend revenue to be recognised only upon contract completion. In the case of a construction contract, the customer receives the promised good or service during construction only if the customer controls the work in progress.

But we believe the definition of control still needs to be clarified in order to be applied consistently. Indeed, the indicators proposed in the ED do not seem to be workable when applied to construction contracts or service arrangements. Finally, we still wonder how an entity would determine when the customer obtains control of the work in progress in a construction contract.

We note that, among the four indicators mentioned in the ED, the "legal title" and "physical possession" indicators are not applicable to service arrangements and are rarely met in construction contracts.

Furthermore, the "unconditional obligation to pay" indicator is, to our mind, difficult to analyse. In construction contracts or service contracts, it is generally unclear whether progress payments are legally unconditional (even if there is a customer acceptance on the work performed to date). Indeed, payments are often subordinated to the final acceptance of the good or service.

In that case, if progress payments are never or marginally redeemed (because there is a customer acceptance on the work performed to date), we propose to consider that this indicator is fulfilled (even if, from a strict legal point of view, it is not easy to assess whether the progress payments are fully unconditional).

Concerning the "customer specific" indicator, we believe it should be fulfilled for most of the contracts defined as in current IAS 11.

Finally, as few indicators are applicable and not one of the indicator determines by itself whether the customer has obtained control, we believe it is difficult to reach a conclusion under the current provisions in the ED.

We think the ED should clarify that if an entity meets the "customer specific" indicator or the "progress payment" indicator (as proposed above), the goods or services are transferred to a customer continuously.

Indeed, we believe that financial statements are more decision-useful to users if revenue associated with construction contracts is recognised continuously over the contract period.

Question 4 — The boards propose that if the amount of consideration is variable, an entity should recognise revenue from satisfying a performance obligation only if the transaction price can be reasonably estimated. Paragraph 38 proposes criteria that an entity should meet to be able to reasonably estimate the transaction price.
Do you agree that an entity should recognise revenue on the basis of an estimated transaction price? If so, do you agree with the criteria in paragraph 38? If not, what approach do you suggest for recognising revenue when the transaction price is variable and why?

We do not agree that an entity should recognise revenue on the basis of the expected value method described in the ED. Rather, we would favour an approach in which revenue is recognised only when it is highly probable.

We do not believe that the expected value method provides useful information to users, because the amount of revenue recognised initially will rarely be the amount of revenue recognised ultimately.

Thus, in example 19, we believe the transaction price should be 110 000 until the entity estimates that the bonus associated with the transaction is highly probable.

Question 5 — Paragraph 43 proposes that the transaction price should reflect the customer's credit risk if its effects on the transaction price can be reasonably estimated. Do you agree that the customer's credit risk should affect how much revenue an entity recognises when it satisfies a performance obligation rather than whether the entity recognises revenue? If not, why?

We agree that the transaction price should reflect the customers' credit risk but do not believe that the effects of the customers' credit risk should affect the revenue line.

Revenue is one of the most important line item in the statement of comprehensive income and it should be understandable for users. Amounts related to credit losses (including changes in the estimated credit risk) should, in our view, be presented separately from revenue.

We understand that credit risk would be presented separately from interest income under the proposals of the ED *Financial instruments amortised cost and impairment*. We do not think credit risk should be presented differently across different standards.

We note that under the proposal of the ED, amounts related to credit losses could affect both the revenue line item and the income or expense line item (once the entity has a receivable). We believe that credit risk may be more difficult to analyse and do not think this result is an improvement for users.

Question 6 — Paragraphs 44 and 45 propose that an entity should adjust the amount of promised consideration to reflect the time value of money if the contract includes a material financing component (whether explicit or implicit). Do you agree? If not, why?

We agree.

Question 7 — Paragraph 50 proposes that an entity should allocate the transaction price to all separate performance obligations in a contract in proportion to the stand-alone selling price (estimated if necessary) of the good or service underlying each of those performance obligations. Do you agree? If not, when and why would that approach not be appropriate and how should the transaction price be allocated in such cases?

We agree with the proposals of the ED.

We understand that the stand alone selling price notion could depend on the customer. For instance, the stand alone selling price of a good or service could depend on the location of the customer. This should be clarified in the definition of the stand alone selling price.

Question 8 — Paragraph 57 proposes that if costs incurred in fulfilling a contract do not give rise to an asset eligible for recognition in accordance with other standards (for example IAS 2 or ASC Topic 330; IAS 16 or ASC Topic 360; and IAS 38 *Intangible Assets* or ASC Topic 985 on software), an entity should recognise an asset only if those costs meet specified criteria.
Do you think that the proposed requirements on accounting for the costs of fulfilling a contract are operational and sufficient? If not, why?

We agree with the proposals of the ED.

Question 9 — Paragraph 58 proposes the costs that relate directly to a contract for the purpose of (a) recognising an asset for resources that the entity would use to satisfy performance obligations in a contract and (b) any additional liability recognised for an onerous performance obligation.
Do you agree with the costs specified? If not, what costs would you include and why?

We agree with the costs specified in § 58 of the ED.

We note that according to § 59, costs of abnormal amounts of wasted materials and labour used to fulfil the contract are expensed as incurred. We believe the Boards should clarify the accounting of costs related to normal "learning curve" incurred in a contract.

In respect of a construction contract in which several identical items are constructed, costs related to the construction of each item may decrease because of growing experience. We

think that the costs related to normal "learning curve" should be capitalised, as they relate directly to the contract and to future performance in the contract and they are not, in our view, costs of abnormal amounts of wasted materials or labour.

Question 10 — The objective of the boards' proposed disclosure requirements is to help users of financial statements understand the amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. Do you think the proposed disclosure requirements will meet that objective? If not, why?
Question 11 — The Boards propose that an entity should disclose the amount of its remaining performance obligations and the expected timing of their satisfaction for contracts with an original duration expected to exceed one year. **Do you agree with that proposed disclosure requirement? If not, what, if any, information do you think an entity should disclose about its remaining performance obligations?**
Question 12 — Do you agree that an entity should disaggregate revenue into the categories that best depict how the amount, timing, and uncertainty of revenue and cash flows are affected by economic factors? If not, why?

We agree with the general provision in the ED that the financial statements should help users to understand the amount, timing and uncertainty of revenue arising from contracts with customers.

We note that disclosures represent more than four pages (in a standard that comprises twenty pages). We believe that the disclosure requirements are excessive and burdensome.

We are not convinced that all the disclosures required in the ED are useful to users, especially:

- the reconciliation of contract balances (§ 75 of the ED) ;
- the disaggregation of revenue (§ 74 of the ED), as this information is partially already required in § 21 of IFRS 8 ;
- the amount of the remaining performance obligations and the expecting timing of their satisfaction (§ 78 of the ED).

We note, as stated in § 70, that "an entity shall consider the level of detail necessary to satisfy the disclosure requirements and how much emphasis to place on each of the various requirements and shall aggregate or disaggregate disclosures so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items that have different characteristics".

To the extent that aggregation of disclosures is allowed when necessary, we agree with the other disclosure requirements proposed in the ED.

We suggest that the Boards as part of their post-implementation review identify unexpected costs or implementation problems encountered on that matter (as planned in the Due Process Handbook).

Question 13 — Do you agree that an entity should apply the proposed requirements retrospectively (that is, as if the entity applied the proposed requirements to all contracts in existence at the effective date and in the comparative period)? If not, why?
Is there an alternative transition method that would preserve trend information about revenue but at a lower cost to preparers? If so, please explain the alternative and why you think it is better.

On the principle, we agree that the final standard should be applied retrospectively. However, we believe this retrospective application may be impracticable (as defined in IAS 8) for entities that conclude very long term contracts. We also recognise that prospective application on new contracts concluded after a fixed date would cause confusion for users and a lack of comparability between entities.

Thus, we would favour some transitional provisions, permitting to apply retrospectively the provisions of the ED only to performance obligations that are being performed or to be performed in the future at the beginning of the earliest comparative period (when practicable). In that case, revenue related to performance obligations already performed at the beginning of the earliest comparative period would not be changed even if some of the performance obligations in the same contract are still being performed or to be performed.

We also believe the timing of recycling of foreign currency hedges could be impacted if revenue is modified. For instance, in a cash flow hedge, if revenue is recognised later under the provisions of the ED than under the current provisions, we believe that the timing of recycling of OCI is modified. In that case, we would also favour some transitional provisions to avoid too much complexity.

Question 14 — The proposed application guidance is intended to assist an entity in applying the principles in the proposed requirements. Do you think that the application guidance is sufficient to make the proposal operational? If not, what additional guidance do you suggest?

As commented above, we believe that the principles in the ED should be clarified before developing additional Application guidance. We do not think that additional guidance can compensate unclear principles.

We think the examples in the Application guidance are oversimplified, especially when they relate to the identification of performance obligations, the determination of whether a good or service is distinct and the transfer of control. There is thus a risk of inconsistent application between entities.

We also question whether the application guidance for buy back is accurate. We do not think the provisions in the *ED Leases* and in the *ED Revenue* are consistent. We think that similar contracts in substance could be accounted differently under the provisions proposed in the EDs.

For instance, if the customer has a put, we understand the customer obtains the control and the entity shall account for the agreement as a sale with a right of return. If the put will be probably exercised (because exercise price is a bargain price), we believe that it should be accounted for as a lease.

We note that if the buy back clause is automatic, it is accounted for as a lease. We question whether an automatic buy back clause and a put clause that will be probably exercised are substantially different transactions and therefore whether they should be accounted differently.

Finally, we believe that AG Example 27 should mention that the method proposed is a way of estimating the value of the option and not the combining of two or more existing contracts (being the contract for the first year and the contracts for the following years).

Question 15 — The Boards propose that an entity should distinguish between the following types of product warranties:

(a) a warranty that provides a customer with coverage for latent defects in the product. This does not give rise to a performance obligation, but requires an evaluation of whether the entity has satisfied its performance obligation to transfer the product specified in the contract.

(b) a warranty that provides a customer with coverage for faults that arise after the

product is transferred to the customer. This gives rise to a performance obligation in addition to the performance obligation to transfer the product specified in the contract.

Do you agree with the proposed distinction between the types of product warranties? Do you agree with the proposed accounting for each type of product warranty? If not, how do you think an entity should account for product warranties and why?

We do not agree with the proposals in the ED related to legal warranties. We do not understand the rationale of the solution proposed in the ED.

We believe all the warranties should be accounted for as separate performance obligations. Especially, there should be no impact on revenue if the warranty costs are reestimated. Considering the difficulties to distinguish between the different types of warranties, this treatment would also be easier to apply for preparers and easier to understand for users.

Should the Boards consider that legal warranties are not separate performance obligations, we believe the entities should account for a provision in accordance with current IAS 37.

Indeed, we believe that the proposed accounting does not work well when the warranty covers defects of products' components. We understand the provisions proposed in the ED would lead to deferring revenue "only for the portion of the transaction price attributed to the product's components expected to be replaced in the repair process" (thus excluding associated costs such as labour in our understanding). We wonder whether labour costs would be recognised under the provisions of IAS 37. In that case, we do not think this treatment will be easy to understand for users.

Question 16 — The boards propose the following if a licence is not considered to be a sale of intellectual property:

(a) **if an entity grants a customer an exclusive licence to use its intellectual property, it has a performance obligation to permit the use of its intellectual property and it satisfies that obligation over the term of the licence; and**

(b) **if an entity grants a customer a non-exclusive licence to use its intellectual property, it has a performance obligation to transfer the licence and satisfies that obligation when the customer is able to use and benefit from the licence.**

Do you agree that the pattern of revenue recognition should depend on whether the licence is exclusive? Do you agree with the patterns of revenue recognition proposed by the boards? Why or why not?

We question whether the "exclusivity" notion is accurate for assessing the transfer of control of a licence. We believe, as explained in the current version of IAS 18, that a licence is in substance a sale when the licensor has no remaining obligation to perform.

We agree with the ED that a licence that is not exclusive should generally be a sale, because the entity has most of the time no remaining obligation to perform.

We are not sure that an exclusive licence to use an intellectual property for substantially all of its economic life is always a sale if the entity has remaining obligations to perform. Conversely, we believe that an exclusive license to use an intellectual property for less than its economic life is a sale if the entity has no remaining obligations to perform.

Question 17 — The boards propose that in accounting for the gain or loss on the sale of some non-financial assets (for example, intangible assets and property, plant and equipment), an entity should apply the recognition and measurement principles of the proposed revenue model. Do you agree? If not, why?

We agree.

Additional issue : definition of a contract

According to the ED, contracts can be implied by the entity's customary business practice. But we also note that an agreement must be enforceable by law to be considered as an existing contract. We would ask the Boards to give additional guidance on the notion of implied contract, as we are not sure to fully understand this notion.