

IASB documents published to accompany**IFRS 15****Revenue from Contracts with Customers**

The text of the unaccompanied standard, IFRS 15, is contained in Part A of this edition. Its effective date when issued was 1 January 2017. In September 2015 the Board issued *Effective Date of IFRS 15* which deferred the effective date to 1 January 2018. The text of the Accompanying Guidance on IFRS 15 is contained in Part B of this edition. This part presents the following documents:

BASIS FOR CONCLUSIONS**DISSENTING OPINION****APPENDICES TO THE BASIS FOR CONCLUSIONS****A Comparison of IFRS 15 and Topic 606****B Amendments to the Basis for Conclusions on other Standards**

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Basis for Conclusions on IFRS 15 Revenue from Contracts with Customers

This Basis for Conclusions accompanies, but is not part of, IFRS 15.

Introduction

- BC1 This Basis for Conclusions summarises the joint considerations of the International Accounting Standards Board (IASB) and the US national standard-setter, the Financial Accounting Standards Board (FASB), in reaching the conclusions in their standards, IFRS 15 *Revenue from Contracts with Customers* and Topic 606, which is introduced into the FASB *Accounting Standards Codification*[®] by the Accounting Standards Update 2014-09 *Revenue from Contracts with Customers*. It includes the reasons for accepting particular views and rejecting others. Individual Board members gave greater weight to some factors than to others.
- BC1A In April 2016, the IASB issued *Clarifications to IFRS 15 Revenue from Contracts with Customers*. The objective of these amendments is to clarify the IASB's intentions when developing the requirements in IFRS 15 but not to change the underlying principles of IFRS 15. Further details are contained in paragraphs BC27A–BC27H. In some cases, the boards made the same amendments to IFRS 15 and Topic 606. In other cases, the boards did not make the same amendments to the standards. The FASB also amended Topic 606 for issues for which the IASB concluded that it was not necessary to amend IFRS 15. The IASB added a further practical expedient to the transition requirements, which the FASB decided not to provide. Accordingly, Appendix A *Comparison of IFRS 15 and Topic 606* to this Basis for Conclusions has been updated to reflect the differences between the amendments to IFRS 15 and the amendments to Topic 606.

Overview

- BC2 IFRS 15 and Topic 606 are the result of the IASB's and the FASB's joint project to improve the financial reporting of revenue under International Financial Reporting Standards (IFRS) and US Generally Accepted Accounting Principles (US GAAP). The boards undertook this project because their requirements for revenue needed improvement for the following reasons:
- (a) US GAAP comprised broad revenue recognition concepts and detailed guidance for particular industries or transactions, which often resulted in different accounting for economically similar transactions.
 - (b) the previous revenue Standards in IFRS had different principles and were sometimes difficult to understand and apply to transactions other than simple ones. In addition, IFRS had limited guidance on important topics such as revenue recognition for multiple-element arrangements. Consequently, some entities that were applying IFRS referred to parts of US GAAP to develop an appropriate revenue recognition accounting policy.

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- (c) the disclosures required under both IFRS and US GAAP were inadequate and often did not provide users of financial statements with information to sufficiently understand revenue arising from contracts with customers.

BC3 IFRS 15 and Topic 606¹ eliminate those inconsistencies and weaknesses by providing a comprehensive revenue recognition model that applies to a wide range of transactions and industries. The comprehensive model also improves previous IFRS and US GAAP by:

- (a) providing a more robust framework for addressing revenue recognition issues;
- (b) improving comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets;
- (c) simplifying the preparation of financial statements by reducing the amount of guidance to which entities must refer; and
- (d) requiring enhanced disclosures to help users of financial statements better understand the nature, amount, timing and uncertainty of revenue that is recognised.

Background

BC4 In December 2008, the boards published for public comment the Discussion Paper *Preliminary Views on Revenue Recognition in Contracts with Customers* and received more than 200 comment letters in response. In the Discussion Paper, the boards proposed the general principles of a contract-based revenue recognition model with a measurement approach that was based on an allocation of the transaction price. That revenue recognition model was developed after extensive discussions by the boards on alternative models for recognising and measuring revenue (see paragraphs BC16–BC27).

BC5 Respondents to the Discussion Paper generally supported the objective of developing a comprehensive revenue recognition model for both IFRS and US GAAP. Most respondents also generally supported the recognition and measurement principles proposed in the Discussion Paper, which are the basic building blocks of the revenue recognition model. In particular, the Discussion Paper introduced the concepts that a contract contains performance obligations for the entity to transfer goods or services to a customer and that revenue is recognised when the entity satisfies its performance obligations as a result of the customer obtaining control of those goods or services.

¹ Unless indicated otherwise, all references to IFRS 15 in this Basis for Conclusions can be read as also referring to Topic 606.

- BC6 Respondents to the Discussion Paper were mainly concerned about the following proposals:
- (a) identifying performance obligations only on the basis of the timing of the transfer of the good or service to the customer. Respondents commented that this would be impractical, especially when many goods or services are transferred over time to the customer (for example, in construction contracts).
 - (b) using the concept of control to determine when a good or service is transferred. Respondents asked the boards to clarify the application of the concept of control to avoid the implication that the proposals would require completed contract accounting for all construction contracts (ie revenue is recognised only when the customer obtains legal title or physical possession of the completed asset).
- BC7 The boards considered those comments when developing the Exposure Draft *Revenue from Contracts with Customers* (the FASB's Exposure Draft was a proposed Accounting Standards Update), which was published in June 2010 (the '2010 Exposure Draft'). Nearly 1,000 comment letters were received from respondents representing a wide range of industries, including construction, manufacturing, telecommunications, technology, pharmaceutical, biotechnology, financial services, consulting, media and entertainment, energy and utilities, freight and logistics, and industries with significant franchising operations, such as hospitality and quick-service restaurant chains. The boards and their staffs also consulted extensively on the proposals in the 2010 Exposure Draft by participating in round-table discussions, conferences, working group sessions, discussion forums and one-to-one discussions that were held across all major geographical regions.
- BC8 The boards also received a substantial number of comment letters in response to a question asked by the FASB on whether the proposals should apply to non-public entities. Almost all of those comment letters were from respondents associated with sections of the US construction industry (for example, private construction contractors, accounting firms that serve those contractors and surety providers who use the financial statements of construction contractors when deciding whether to guarantee that those contractors will meet their obligations under a contract). Those respondents also raised concerns about the application of the proposed model to non-public entities. Those issues were considered and discussed separately by the FASB.
- BC9 With the exception of many of the responses from non-public entities in the construction industry, most of the feedback from the comment letters and from the consultation activities generally supported the boards' proposal for a comprehensive revenue recognition model for both IFRS and US GAAP. Moreover, most respondents supported the core principle of that model, which was that an entity should recognise revenue to depict the transfer of goods or services to a customer in an amount that reflects the amount of consideration that the entity expects to receive for those goods or services.

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- BC10 Almost all respondents to the 2010 Exposure Draft indicated that the boards should clarify further the operation of the core principle. In particular, respondents were concerned about the application of the following:
- (a) the concept of control and, in particular, the application of the indicators of the transfer of control to service contracts and to contracts for the transfer of an asset over time to a customer as it is being constructed (for example, a work-in-progress asset).
 - (b) the principle of distinct goods or services for identifying performance obligations in a contract. Many respondents were concerned that the proposed principle would lead to inappropriate disaggregation of the contract.
- BC11 The boards addressed those concerns during the redeliberations of the proposals in the 2010 Exposure Draft. As the redeliberations of those proposals drew to a close, the boards decided to issue a revised Exposure Draft for public comment to provide interested parties with an opportunity to comment on the revisions that the boards had made since the 2010 Exposure Draft was published. The boards decided unanimously that it was appropriate to go beyond their established due process and re-expose their revised revenue proposals, because of the importance of revenue to all entities and to avoid unintended consequences in the recognition of revenue for specific contracts or industries. The revised Exposure Draft *Revenue from Contracts with Customers* was published in November 2011 (the '2011 Exposure Draft') and approximately 350 comment letters were received from respondents representing a wide range of industries. As in the case of the 2010 Exposure Draft, the boards and their staffs consulted extensively on the proposals in the 2011 Exposure Draft. This consultation also included all major geographical regions and occurred in a number of formats. Many of the discussions focused on detailed analyses related to the application of the revenue recognition model and the principles in the 2011 Exposure Draft.
- BC12 Almost all respondents continued to support the core principle of the revenue recognition model, which is that an entity should recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Moreover, most of the feedback from the comment letters and from the consultation activities generally supported the revisions to the boards' proposed revenue recognition model in the 2011 Exposure Draft. However, respondents raised issues or questions on some of the proposals in the 2011 Exposure Draft. That feedback could be broadly divided into three categories:
- (a) requests for clarifications and further refinements—such as on the criteria for identifying performance obligations, determining when a performance obligation is satisfied over time and constraining estimates of variable consideration;

- (b) difficulties in the practical application of the requirements—such as on the time value of money (referred to as a significant financing component in IFRS 15) and the retrospective application of the proposed Standard; and
- (c) disagreement with some of the proposed requirements for the following topics:
 - (i) identifying onerous performance obligations;
 - (ii) disclosing information about revenue;
 - (iii) applying the requirements for licences; and
 - (iv) applying the allocation principles to contracts that are prevalent in the telecommunications industry.

BC13 The boards addressed those concerns during the redeliberations of the proposals in the 2011 Exposure Draft. The boards' discussion of those concerns and their conclusions are included in the relevant sections of this Basis for Conclusions.

Why make the change?

BC14 Throughout the project, some respondents questioned the need to replace the requirements for revenue recognition, particularly because those requirements seemed to work reasonably well in practice and provided useful information about the different types of contracts for which they were intended.

- (a) For US GAAP, some questioned whether a new revenue recognition model was necessary, because Accounting Standards Update No. 2009-13 *Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements* resolved some of the issues that the Revenue Recognition project had originally intended to resolve. Furthermore, the *FASB Accounting Standards Codification*[®] (the Codification) had simplified the process of accessing and researching previous requirements for revenue.
- (b) For IFRS, some indicated that the IASB could have improved, rather than replace, its previous revenue Standards by developing additional requirements for critical issues (for example, multiple-element arrangements).

BC15 The boards acknowledged that it would have been possible to improve many of the previous revenue recognition requirements without replacing them. However, even after the changes to US GAAP mentioned in paragraph BC14(a), the requirements in US GAAP would have continued to result in inconsistent accounting for revenue and, consequently, would not have provided a robust framework for addressing revenue recognition issues in the future. Furthermore, amending the requirements would have failed to achieve one of the goals of the Revenue Recognition project, which was to develop a common revenue standard for IFRS and US GAAP that entities could apply consistently across industries, jurisdictions and capital markets. Because revenue is a

crucial number to users of financial statements, the boards decided that a common standard on revenue for IFRS and US GAAP is an important step toward achieving the goal of a single set of high-quality global accounting standards. To be consistent with that goal, the boards noted that previous revenue recognition requirements in IFRS and US GAAP should not be used to supplement the principles in IFRS 15.

Alternative revenue recognition models

BC16 During the early stages of their Revenue Recognition project, the boards considered various alternative revenue recognition models, including the following:

- (a) the basis for recognising revenue—specifically, whether an entity should recognise revenue only when it transfers a promised good or service to a customer (a contract-based revenue recognition principle) or when (or as) the entity undertakes a productive activity (which could be an activity that is undertaken regardless of whether a contract exists); and
- (b) the basis for measuring revenue—specifically, whether revenue should be measured at an allocated customer consideration amount (ie the transaction price) or at a current exit price.

Basis for recognising revenue

BC17 In the Discussion Paper, the boards proposed a principle to recognise revenue on the basis of the accounting for the asset or the liability arising from a contract with a customer. The boards had two reasons for developing a standard on revenue that applies only to contracts with customers. First, contracts to provide goods or services to customers are important economic phenomena and are crucial to most entities. Second, most previous revenue recognition requirements in IFRS and US GAAP focused on contracts with customers. The boards decided that focusing on the recognition and measurement of the asset or liability arising from a contract with a customer and the changes in that asset or liability over the life of the contract would bring discipline to the earnings process approach. Consequently, it would result in entities recognising revenue more consistently than they did under previous revenue recognition requirements.

BC18 Upon entering into a contract with a customer, an entity obtains rights to receive consideration from the customer and assumes obligations to transfer goods or services to the customer (performance obligations). The combination of those rights and performance obligations gives rise to a (net) asset or a (net) liability depending on the relationship between the remaining rights and the performance obligations. The contract is an asset (a contract asset) if the measure of the remaining rights exceeds the measure of the remaining performance obligations. Conversely, the contract is a liability (a contract liability) if the measure of the remaining performance obligations exceeds the measure of the remaining rights.

- BC19 By definition, revenue from a contract with a customer cannot be recognised until a contract exists. Conceptually, revenue recognition could occur at the point at which an entity enters into a contract with a customer. For an entity to recognise revenue at contract inception (before either party has performed), the measure of the entity's rights must exceed the measure of the entity's performance obligations. This could occur if the rights and obligations were measured at current exit prices and would lead to revenue recognition because of an increase in a contract asset. However, as described in paragraph BC25, the boards proposed in the Discussion Paper that performance obligations should be measured at the same amount as the rights in the contract at contract inception, thereby precluding the recognition of a contract asset and revenue at contract inception.
- BC20 Therefore, the boards decided 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. That transfer results in revenue recognition, because upon satisfying a performance obligation an entity no longer has that obligation to provide the good or service. Consequently, its position in the contract increases—either its contract asset increases or its contract liability decreases—and that increase leads to revenue recognition.
- BC21 Although, conceptually, revenue arises from an increase in a contract asset or a decrease in a contract liability, the boards articulated the requirements in terms of the recognition and measurement of revenue rather than the recognition and measurement of the contract. The boards noted that focusing on the timing and amount of revenue from a contract with a customer would simplify the requirements. Feedback from respondents to the Discussion Paper and the 2010 and 2011 Exposure Drafts confirmed that view.
- BC22 Nearly all respondents to the Discussion Paper agreed with the boards' view that an entity generally should not recognise revenue if there is no contract with a customer. However, some respondents requested that the boards instead develop an activities model in which revenue would be recognised as the entity undertakes activities in producing or providing goods or services, regardless of whether those activities result in the transfer of goods or services to the customer. Those respondents reasoned that recognising revenue over time, for example, throughout long-term construction or other service contracts, regardless of whether goods or services are transferred to the customer, would provide users of financial statements with more useful information.
- BC23 However, the boards noted the following concerns about an activities model:
- (a) revenue recognition would not have been based on accounting for the contract. In an activities model, revenue arises from increases in the entity's assets, such as inventory or work-in-progress, rather than only from rights under a contract. Consequently, conceptually, an activities model does not require a contract with a customer for revenue recognition, although revenue recognition could be precluded until a contract exists. However, that would have resulted in revenue being

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recognised at contract inception for any activities completed to that point.

- (b) it would have been counterintuitive to many users of financial statements. An entity would have recognised consideration as revenue when the customer had not received any promised goods or services in exchange.
- (c) there would have been potential for abuse. An entity could have accelerated revenue recognition by increasing its activities (for example, production of inventory) at the end of a reporting period.
- (d) it would have resulted in a significant change to previous revenue recognition requirements and practices. In many of those requirements, revenue was recognised only when goods or services were transferred to the customer. For example, previous requirements in IFRS required revenue from the sale of a good to be recognised when the entity transferred ownership of the good to the customer. The boards also observed that the basis for percentage-of-completion accounting in previous revenue recognition requirements could be viewed as similar to the core principle in IFRS 15.

BC24 Accordingly, the boards did not develop an activities model and they maintained their view that a contract-based revenue recognition principle is the most appropriate principle for a general revenue recognition standard for contracts with customers.

Basis for measuring revenue

BC25 The boards decided that an allocated transaction price approach should be applied to measure performance obligations. Using that approach, an entity would allocate the transaction price to each performance obligation in the contract (see paragraphs BC181 and BC266). In the Discussion Paper, the boards considered an alternative approach to measure performance obligations directly at current exit prices. However, the boards rejected that approach for the following reasons:

- (a) an entity would have recognised revenue before transferring goods or services to the customer at contract inception if the measure of rights to consideration exceeded the measure of the remaining performance obligations. That would have been a typical occurrence at contract inception, because the transaction price often includes amounts that enable an entity to recover its costs to obtain a contract.
- (b) any errors in identifying or measuring performance obligations could have affected revenue recognised at contract inception.
- (c) a current exit price (ie the price that would be received to sell an asset or paid to transfer a liability) for the remaining performance obligations is typically not observable and an estimated current exit price could be complex and costly to prepare and difficult to verify.

BC26 Almost all respondents supported the boards' proposal to measure performance obligations using an allocated transaction price approach.

BC27 In the Discussion Paper, the boards also considered whether it would be appropriate to require an alternative measurement approach for some types of performance obligations (for example, performance obligations with highly variable outcomes, for which an allocated transaction price approach may not result in useful information). However, the boards decided that the benefits of accounting for all performance obligations within the scope of the requirements using the same measurement approach outweighed any concerns about using that approach for some types of performance obligations. The boards also noted that a common type of contract with customers that has highly variable outcomes would be an insurance contract, which is excluded from the scope of IFRS 15.

Clarifications to IFRS 15 (amendments issued in April 2016)

BC27A After issuing IFRS 15 and Topic 606 in May 2014, the boards formed the Transition Resource Group (TRG) for Revenue Recognition to support implementation of these standards. One of the objectives of the TRG is to inform the boards about implementation issues to help the boards determine what, if any, action should be undertaken to address those issues. The substantial majority of the submissions from stakeholders regarding the implementation of IFRS 15, as discussed by the TRG, were determined to be sufficiently addressed by the requirements in IFRS 15. However, the TRG's discussions on five topics indicated potential differences of views on how to implement the requirements and, therefore, were considered by the boards. Those topics were:

- (a) identifying performance obligations;
- (b) principal versus agent considerations;
- (c) licensing;
- (d) collectability; and
- (e) measuring non-cash consideration.

BC27B The boards also received requests from some stakeholders for practical expedients in respect of the following:

- (a) accounting for contract modifications that occurred before transition to IFRS 15;
- (b) for entities electing to use the full retrospective transition method, accounting for a contract completed under previous revenue Standards before transition to IFRS 15; and
- (c) assessing whether a sales tax (or a similar tax) is collected on behalf of a third party.

BC27C The boards discussed the five topics and the possible practical expedients, and each board decided to make amendments to clarify the requirements in IFRS 15 and Topic 606 respectively. As a result, the IASB issued *Clarifications to IFRS 15* in April 2016 making targeted amendments to IFRS 15 with respect to

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three of the five topics considered—identifying performance obligations, principal versus agent considerations and licensing. The IASB concluded that it was not necessary to amend IFRS 15 with respect to the other two topics—collectability and measuring non-cash consideration. In respect of the practical expedients, the IASB provided transition relief for modified contracts and completed contracts.

BC27D In reaching its conclusions to make clarifying amendments and provide transition relief to IFRS 15, the IASB considered the need to balance being responsive to issues raised to help entities implement IFRS 15 but, at the same time, not creating a level of uncertainty about IFRS 15 to the extent that the IASB's actions might be disruptive to the implementation process. The IASB noted that, when new Standards are issued, there are always initial questions that arise. Those questions are generally resolved as entities, auditors and others work through them over time, and gain a better understanding of the new requirements. The IASB also considered the effect of any differences between its decisions and those made by the FASB.

BC27E With these wider considerations in mind, the IASB decided to apply a high hurdle when considering whether to amend IFRS 15 and, thus, to minimise changes to the extent possible. On this basis, the IASB made clarifying amendments to IFRS 15 only when (a) it considered those amendments to be essential to clarifying the IASB's intentions when developing the requirements in IFRS 15; or (b) it viewed the benefits of retaining converged requirements as greater than any potential costs of amending the requirements.

BC27F The FASB decided to make more extensive amendments to Topic 606, as explained in paragraph BC27G. The FASB issued amendments to the application guidance in Topic 606 on principal versus agent considerations, Accounting Standards Update (ASU) 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)*, in March 2016. The FASB is expected to issue two further ASUs:

- (a) one ASU for its amendments to the requirements with respect to identifying performance obligations and the application guidance on licensing; and
- (b) another ASU for its amendments to the requirements in Topic 606 with respect to the other topics and the practical expedients.

BC27G The FASB's amendments to Topic 606 are the same as the IASB's amendments to IFRS 15 with respect to (a) the requirements on identifying performance obligations relating to the determination of whether an entity's promise to transfer a good or service to a customer is distinct within the context of the contract; and (b) the application guidance on principal versus agent considerations. The FASB made further amendments regarding some other requirements on identifying performance obligations. In relation to licensing, the boards made the same clarifying amendments for sales-based and usage-based royalties. The boards decided to make different amendments to the application guidance relating to identifying the nature of an entity's promise in granting a licence. The FASB also decided to amend Topic 606 for other issues relating to licensing for which the IASB decided not to make any

amendments to IFRS 15. The FASB has also decided (a) to amend Topic 606 with respect to collectability and measuring non-cash consideration and (b) to provide an accounting policy election to present all sales taxes on a net basis. The FASB decided to provide similar transition relief to that provided in IFRS 15 for contract modifications. However, with respect to completed contracts, the FASB decided to (a) amend the definition of a completed contract; and (b) provide transition relief, similar to the relief provided by the IASB, only for entities that apply Topic 606 in accordance with paragraph 606-10-65-1(d)(2) (equivalent to paragraph C3(b) of IFRS 15).

BC27H Because of the different decisions of the boards, Appendix A *Comparison of IFRS 15 and Topic 606* to this Basis for Conclusions has been updated. The IASB's considerations together with an overview of the FASB's considerations (based on both the amendments to Topic 606 issued and decisions made by the FASB until March 2016) in reaching their respective decisions are explained in the following paragraphs.

Topics for which both the IASB and FASB decided to amend IFRS 15 and Topic 606

Topic	Reference
Identifying performance obligations	paragraphs BC116A–BC116U
Principal versus agent considerations	paragraphs BC385A–BC385Z
Licensing	paragraphs BC414A–BC414Y paragraphs BC421A–BC421J
Practical expedients on transition	paragraphs BC445A–BC445B paragraphs BC445J–BC445R

Topics for which the IASB decided not to amend IFRS 15 but the FASB decided to amend Topic 606

Topic	Reference
Collectability	paragraphs BC46A–BC46H
Presentation of sales taxes (determining the transaction price)	paragraphs BC188A–BC188D
Non-cash consideration	paragraphs BC254A–BC254H
Definition of a completed contract	paragraphs BC445C–BC445I

Scope

BC28 The boards decided that IFRS 15 should apply only to a subset of revenue as defined in each of the boards' conceptual frameworks (ie revenue from contracts with customers). Revenue from transactions or events that does not arise from a contract with a customer is not within the scope of IFRS 15 and, therefore, those transactions or events will continue to be recognised in accordance with other Standards, for example:

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- (a) dividends received (although these requirements existed in previous revenue Standards in IFRS, the IASB has moved them unchanged, and without changing their effect, into IFRS 9 *Financial Instruments*);
- (b) non-exchange transactions (for example, donations or contributions received);
- (c) for IFRS, changes in the value of biological assets, investment properties and the inventory of commodity broker-traders; and
- (d) for US GAAP, changes in regulatory assets and liabilities arising from alternative revenue programmes for rate-regulated entities in the scope of Topic 980 on regulated operations. (The FASB decided that the revenue arising from those assets or liabilities should be presented separately from revenue arising from contracts with customers. Therefore, the FASB made amendments to Subtopic 980-605 *Regulated Operations – Revenue Recognition*.)

BC29 The boards decided not to amend the existing definitions of revenue in each of their conceptual frameworks. The boards decided that they will consider the definition of revenue when they revise their respective conceptual frameworks. However, the IASB decided to carry forward into IFRS 15 the description of revenue from the IASB's *Conceptual Framework for Financial Reporting*² rather than the definition of revenue from a previous revenue Standard. The IASB noted that the definition in a previous revenue Standard referred to 'gross inflow of economic benefits' and it had concerns that some might have misread that reference as implying that an entity should recognise as revenue a prepayment from a customer for goods or services. As described in paragraphs BC17–BC24, the principle is that revenue is recognised in accordance with IFRS 15 as a result of an entity satisfying a performance obligation in a contract with a customer. In addition, the FASB decided to carry forward a definition of revenue that is based on the definition in FASB Concepts Statement No. 6 *Elements of Financial Statements*.

BC30 The converged definitions of a contract and a customer establish the scope of IFRS 15.

Definition of a contract (Appendix A)

BC31 The boards' definition of contract is based on common legal definitions of a contract in the United States and is similar to the definition of a contract used in IAS 32 *Financial Instruments: Presentation*. The IASB decided not to adopt a single definition of a contract for both IAS 32 and IFRS 15, because the IAS 32 definition implies that contracts can include agreements that are not enforceable by law. Including such agreements would have been inconsistent with the boards' decision that a contract with a customer must be enforceable by law for an entity to recognise the rights and obligations arising from that contract. The IASB also noted that amending the IAS 32 definition would have

² References to the *Conceptual Framework* in this Basis for Conclusions are to the *Conceptual Framework for Financial Reporting*, issued in 2010 and in effect when the Standard was developed.

posed the risk of unintended consequences in accounting for financial instruments.

BC32 The definition of a contract emphasises that a contract exists when an agreement between two or more parties creates enforceable rights and obligations between those parties. The boards noted that the agreement does not need to be in writing to be a contract. Whether the agreed-upon terms are written, oral or evidenced otherwise (for example, by electronic assent), a contract exists if the agreement creates rights and obligations that are enforceable against the parties. Determining whether a contractual right or obligation is enforceable is a question to be considered within the context of the relevant legal framework (or equivalent framework) that exists to ensure that the parties' rights and obligations are upheld. The boards observed that the factors that determine enforceability may differ between jurisdictions. Although there must be enforceable rights and obligations between parties for a contract to exist, the boards decided that the performance obligations within the contract could include promises that result in the customer having a valid expectation that the entity will transfer goods or services to the customer even though those promises are not enforceable (see paragraph BC87).

BC33 The boards decided to complement the definition of a contract by specifying criteria that must be met before an entity can apply the revenue recognition model to that contract (see paragraph 9 of IFRS 15). Those criteria are derived mainly from previous revenue recognition requirements and other existing standards. The boards decided that when some or all of those criteria are not met, it is questionable whether the contract establishes enforceable rights and obligations. The boards' rationale for including those criteria is discussed in paragraphs BC35–BC46.

BC34 The boards also decided that those criteria would be assessed at contract inception and would not be reassessed unless there is an indication that there has been a significant change in facts and circumstances (see paragraph 13 of IFRS 15). The boards decided that it was important to reassess the criteria in those cases, because that change might clearly indicate that the remaining contractual rights and obligations are no longer enforceable. The word 'remaining' in paragraph 13 of IFRS 15 indicates that the criteria would be applied only to those rights and obligations that have not yet transferred. That is, an entity would not include in the reassessment (and therefore would not reverse) any receivables, revenue or contract assets already recognised.

The parties have approved the contract and are committed to perform their respective obligations (paragraph 9(a))

BC35 The boards decided to include this criterion because if the parties to a contract have not approved the contract, it is questionable whether that contract is enforceable. Some respondents questioned whether oral and implied contracts could meet this criterion, especially if it is difficult to verify an entity's approval of that contract. The boards noted that the form of the contract does not, in and of itself, determine whether the parties have approved the contract. Instead, an entity should consider all relevant facts and circumstances in assessing whether the parties intend to be bound by the

terms and conditions of the contract. Consequently, in some cases, the parties to an oral or an implied contract (in accordance with customary business practices) may have agreed to fulfil their respective obligations. In other cases, a written contract may be required to determine that the parties to the contract have approved it.

- BC36 In addition, the boards decided that the parties should be committed to performing their respective obligations under the contract. However, the boards decided that an entity and a customer would not always need to be committed to fulfilling all of their respective rights and obligations for a contract to meet the requirements in paragraph 9(a) of IFRS 15. For example, a contract might include a requirement for the customer to purchase a minimum quantity of goods from the entity each month, but the customer's past practice indicates that the customer is not committed to always purchasing the minimum quantity each month and the entity does not enforce the requirement to purchase the minimum quantity. In that example, the criterion in paragraph 9(a) of IFRS 15 could still be satisfied if there is evidence that demonstrates that the customer and the entity are substantially committed to the contract. The boards noted that requiring all of the rights and obligations to be fulfilled would have inappropriately resulted in no recognition of revenue for some contracts in which the parties are substantially committed to the contract.

The entity can identify each party's rights regarding the goods or services to be transferred (paragraph 9(b))

- BC37 The boards decided to include this criterion because an entity would not be able to assess the transfer of goods or services if it could not identify each party's rights regarding those goods or services.

The entity can identify the payment terms for the goods or services to be transferred (paragraph 9(c))

- BC38 The boards decided to include this criterion because an entity would not be able to determine the transaction price if it could not identify the payment terms in exchange for the promised goods or services.

- BC39 Respondents from the construction industry questioned whether an entity can identify the payment terms for orders for which the scope of work may already have been defined even though the specific amount of consideration for that work has not yet been determined and may not be finally determined for a period of time (sometimes referred to as unpriced change orders or claims). The boards clarified that their intention is not to preclude revenue recognition for unpriced change orders if the scope of the work has been approved and the entity expects that the price will be approved. The boards noted that, in those cases, the entity would consider the requirements for contract modifications (see paragraphs BC76–BC83).

The contract has commercial substance (paragraph 9(d))

- BC40 The boards decided to include ‘commercial substance’ as a criterion when they discussed whether revenue should be recognised in contracts with customers that include non-monetary exchanges. Without that requirement, entities might transfer goods or services back and forth to each other (often for little or no cash consideration) to artificially inflate their revenue. Consequently, the boards decided that an entity should not recognise revenue from a non-monetary exchange if the exchange has no commercial substance.
- BC41 The boards decided to describe commercial substance in paragraph 9(d) of IFRS 15 in a manner that is consistent with its existing meaning in other financial reporting contexts, such as existing requirements for non-monetary exchange transactions. The boards also observed that this criterion is important in all contracts (not only non-monetary exchanges) because without commercial substance it is questionable whether an entity has entered into a transaction that has economic consequences. Consequently, the boards decided that all contracts should have commercial substance before an entity can apply the other requirements in the revenue recognition model.

It is probable that the entity will collect the consideration to which it will be entitled (paragraph 9(e))

- BC42 The boards included the criterion in paragraph 9(e) of IFRS 15 (which acts like a collectability threshold) because they concluded that the assessment of a customer’s credit risk was an important part of determining whether a contract is valid. Furthermore, the boards decided to include this criterion as a consequence of their decision that customer credit risk should not affect the measurement or presentation of revenue (see paragraphs BC259–BC265).
- BC43 The boards decided that a collectability threshold is an extension of the other requirements in paragraph 9 of IFRS 15 on identifying the contract. In essence, the other criteria in paragraph 9 require an entity to assess whether the contract is valid and represents a genuine transaction. The collectability threshold is related to that assessment because a key part of assessing whether a transaction is valid is determining the extent to which the customer has the ability and the intention to pay the promised consideration. In addition, entities generally only enter into contracts in which it is probable that the entity will collect the amount to which it will be entitled.
- BC44 The boards noted that the term ‘probable’ has different meanings under US GAAP and IFRS. Under US GAAP, the term was initially defined in Topic 450 *Contingencies* as ‘likely to occur’ whereas under IFRS, probable is defined as ‘more likely than not’. The boards noted that using the same term which has different meanings in US GAAP and IFRS could result in accounting that is not converged when determining whether the criterion in paragraph 9(e) of IFRS 15 is met. However, the boards noted that the term ‘probable’ was used in some of the collectability thresholds in their previous revenue recognition requirements and both boards wanted to maintain consistency with those requirements. (The term ‘reasonably assured’ was also used in collectability thresholds in some parts of US GAAP. However, in this context, the FASB understood that in practice, probable and reasonably

assured had similar meanings.) In addition, the boards observed that in most transactions, an entity would not enter into a contract with a customer in which there was significant credit risk associated with that customer without also having adequate economic protection to ensure that it would collect the consideration. Consequently, the boards decided that there would not be a significant practical effect of the different meaning of the same term because the population of transactions that would fail to meet the criterion in paragraph 9(e) of IFRS 15 would be small.

BC45 In determining whether it is probable that an entity will collect the amount of consideration to which the entity will be entitled, an entity might first need to determine the amount of consideration to which the entity will be entitled. This is because, in some circumstances, the amount of consideration to which an entity will be entitled may be less than the price stated in the contract. This could be because the entity might offer the customer a price concession (see paragraph 52 of IFRS 15) or because the amount of consideration to which an entity will be entitled varies for other reasons, such as the promise of a bonus. In either of those circumstances, an entity considers whether it is probable that the entity will collect the amount of consideration to which it will be entitled when the uncertainty relating to that consideration is resolved. The entity assesses whether it is probable of collecting that amount by considering both of the following:

- (a) the ability (ie the financial capacity) of the customer to pay the amount of consideration to which the entity will be entitled in exchange for the goods or services transferred.
- (b) the customer's intention to pay that amount. The boards observed that an assessment of the customer's intention would require an entity to consider all of the facts and circumstances, including the past practice of that customer or customer class. The boards noted that this assessment should be made on the assumption that the amount will be due (ie the corresponding performance obligation will be satisfied and the consideration is not subject to further variability that might affect the entity's entitlement to that consideration).

BC46 In addition, the boards specified in paragraph 9(e) of IFRS 15 that an entity should assess only the consideration to which it will be entitled in exchange for the goods or services that will be transferred to a customer. Therefore, if the customer were to fail to perform as promised and consequently the entity would respond to the customer's actions by not transferring any further goods or services to the customer, the entity would not consider the likelihood of payment for those goods or services that would not be transferred.

Clarifications to IFRS 15 (amendments issued in April 2016)—topics for which the IASB decided not to amend IFRS 15

BC46A The TRG discussed an implementation question raised by stakeholders about how to apply the collectability criterion in paragraph 9(e) of IFRS 15 in instances in which the entity has received non-refundable consideration from a customer assessed as having poor credit quality. The discussion informed the boards that there are potentially different interpretations of:

- (a) how to apply the collectability criterion in paragraph 9(e) when it is not probable that the total consideration promised in the contract is collectable; and
- (b) when to recognise the non-refundable consideration received from the customer as revenue in accordance with paragraph 15 of IFRS 15 when the contract does not meet the criteria in paragraph 9 of IFRS 15.

Assessing collectability

- BC46B Paragraph 9(e) requires an entity to assess whether it is probable that it will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. This assessment forms part of Step 1 of IFRS 15 *Identify the contract(s) with a customer*. The TRG's discussions informed the boards that some stakeholders interpreted this requirement to mean that an entity should assess the probability of collecting all of the consideration promised in the contract. Under this interpretation, some contracts with customers that are assessed as having poor credit quality would not meet the criteria in paragraph 9(e), even though they are otherwise valid contracts. Other stakeholders asserted that those contracts would be valid if the entity has the ability to protect itself from credit risk.
- BC46C The boards noted that the assessment in paragraph 9(e) requires an entity to consider how the entity's contractual rights to the consideration relate to its performance obligations. That assessment considers the entity's exposure to the customer's credit risk and the business practices available to the entity to manage its exposure to credit risk throughout the contract. For example, an entity may be able to stop providing goods or services to the customer or require advance payments. This is consistent with the explanation of the boards' considerations as described in paragraph BC46.
- BC46D The FASB decided to amend the implementation guidance and illustrations in Topic 606 to clarify that an entity should assess the collectability of the consideration promised in a contract for the goods or services that will be transferred to the customer rather than assessing the collectability of the consideration promised in the contract for all of the promised goods or services.
- BC46E Having considered the wider implications of amending IFRS 15 before its effective date, the IASB concluded that the existing requirements in IFRS 15 and the explanations in paragraphs BC42–BC46 are sufficient. The IASB noted that it expects practice to develop consistently with the boards' intentions in developing the collectability criterion in paragraph 9(e). The IASB does not expect the FASB's anticipated clarifications to the paragraph equivalent to paragraph 9(e) in Topic 606 to result in any additional differences in outcomes. In reaching its decision, the IASB observed that an entity will generally not enter into a contract with a customer if the entity does not consider it to be probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. This is consistent with the boards' reasoning in paragraph BC43. It was not the boards' intention that many contracts should fail the condition in paragraph 9(e). On this basis, the IASB thinks that the

population of contracts to which any clarification to paragraph 9(e) might apply is small.

Contract termination

- BC46F Paragraph 15 specifies when an entity should recognise any consideration received from a customer as revenue when the contract does not meet Step 1 of the revenue recognition model. Paragraph 15(b) states that an entity should recognise revenue when the contract has been terminated and the consideration received from the customer is non-refundable. The TRG's discussions informed the boards about potential diversity in stakeholders' understanding of when a contract is terminated. The assessment of when a contract is terminated affects when an entity recognises revenue in a contract that does not meet Step 1 of the revenue recognition model. Some stakeholders asserted that a contract is terminated when an entity stops transferring promised goods or services to the customer. Other stakeholders asserted that a contract is terminated only when the entity stops pursuing collection from the customer. Stakeholders noted that those two events often occur at different points in time. For example, entities sometimes pursue collection for a significant period of time after they have stopped transferring promised goods or services to the customer. As a result, non-refundable consideration received from the customer might be recognised as a liability for a significant period of time during which an entity pursues collection, even though the entity may have stopped transferring promised goods or services to the customer and has no further obligations to transfer goods or services to the customer.
- BC46G The FASB decided to amend paragraph 606-10-25-7 of Topic 606 (equivalent to paragraph 15 of IFRS 15) to add an additional event in which an entity should recognise any consideration received as revenue. This amendment is expected to allow an entity to recognise any consideration received as revenue when (a) the entity has transferred control of the goods or services to which the consideration received relates; (b) the entity has stopped transferring additional goods or services and has no obligation to transfer additional goods or services; and (c) the consideration received from the customer is non-refundable.
- BC46H The IASB noted that contracts often specify that an entity has the right to terminate the contract in the event of non-payment by the customer and that this would not generally affect the entity's rights to recover any amounts owed by the customer. The IASB also noted that an entity's decision to stop pursuing collection would not typically affect the entity's rights and the customer's obligations under the contract with respect to the consideration owed by the customer. On this basis, the IASB concluded that the existing requirements in IFRS 15 are sufficient for an entity to conclude, without any additional clarification, that a contract is terminated when it stops providing goods or services to the customer. Some IASB members also expressed concerns about the potential for unintended consequences relating to other areas of IFRS if contract termination were to be defined in IFRS 15. Consequently, the IASB decided not to amend paragraph 15.

Accounting for contracts that do not meet the criteria in paragraph 9

- BC47 The boards decided to include the requirements in paragraphs 14–16 of IFRS 15 in response to questions from some respondents about how an entity should account for its rights and obligations when a contract does not meet the criteria in paragraph 9 of IFRS 15. Those respondents were concerned that if a contract did not meet the criteria in paragraph 9 of IFRS 15, in the absence of specific requirements, an entity would seek alternative guidance and potentially apply the revenue recognition model by analogy, which might not result in appropriate accounting. Consequently, the boards specified that in cases in which the contract does not meet the criteria in paragraph 9 of IFRS 15, an entity should recognise the consideration received as revenue only when one of the events in paragraph 15 of IFRS 15 has occurred or the entity reassesses the criteria in paragraph 9 of IFRS 15 and the contract subsequently meets those criteria.
- BC48 The requirements in paragraph 15 are consistent with the boards' rationale for paragraph 9 of IFRS 15, which is to filter out contracts that may not be valid and that do not represent genuine transactions, and therefore recognising revenue for those contracts would not provide a faithful representation of such transactions. The requirements therefore preclude an entity from recognising any revenue until the contract is either complete or cancelled or until a subsequent reassessment indicates that the contract meets all of the criteria in paragraph 9 of IFRS 15. The boards noted that this approach is similar to the 'deposit method' that was previously included in US GAAP and that was applied when there was no consummation of a sale.
- BC49 The boards considered whether to include asset derecognition requirements (and therefore cost recognition requirements) for assets related to a contract that does not meet the criteria in paragraph 9 of IFRS 15. However, the boards decided not to include requirements for asset derecognition for these types of transactions, because including those requirements would be outside the scope of this project. (However, the FASB added some asset derecognition guidance to other Standards for transactions outside the scope of the requirements—that is, for the transfer of non-financial assets. See paragraphs BC494–BC503.) The boards noted that entities should apply existing IFRS and US GAAP to assets related to contracts that do not meet the criteria in paragraph 9 of IFRS 15.

Wholly unperformed contracts

- BC50 The boards decided that IFRS 15 should not apply to wholly unperformed contracts if each party to the contract has the unilateral enforceable right to terminate the contract without penalty. Those contracts would not affect an entity's financial position or performance until either party performs. In contrast, there could be an effect on an entity's financial position and performance if only one party could terminate a wholly unperformed contract without penalty. For instance, if only the customer could terminate the wholly unperformed contract without penalty, the entity is obliged to stand ready to perform at the discretion of the customer. Similarly, if only the entity

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could terminate the wholly unperformed contract without penalty, it has an enforceable right to payment from the customer if it chooses to perform.

- BC51 In accordance with IFRS 15, an entity's rights and obligations in wholly unperformed non-cancellable contracts are measured at the same amount and, therefore, would offset each other at inception. However, by including those contracts within the scope of IFRS 15, an entity would provide additional information about a change in its financial position that resulted from entering into those contracts, that is, disclosing the amount of transaction price allocated to the remaining performance obligations in that wholly unperformed contract (see paragraph 120 of IFRS 15).

Definition of a customer (paragraph 6 and Appendix A)

- BC52 The boards decided to define the term 'customer' to enable an entity to distinguish contracts that should be accounted for under IFRS 15 (ie contracts with customers) from contracts that should be accounted for under other requirements.

- BC53 The definition of a customer in IFRS 15 refers to an entity's ordinary activities. Some respondents asked the boards to clarify the meaning of ordinary activities; however, the boards decided not to provide additional requirements, because the notion of ordinary activities is derived from the definitions of revenue in the boards' respective conceptual frameworks. In particular, the IASB's *Conceptual Framework* description of revenue refers specifically to the 'ordinary activities of an entity' and the definition of revenue in FASB Concepts Statement No. 6 refers to the notion of an entity's 'ongoing major or central operations'. As noted in paragraph BC29, the boards did not reconsider those definitions as part of the Revenue Recognition project.

- BC54 Some respondents asked the boards to clarify whether the parties to some common types of contracts (for example, contracts with collaborators or partners) would meet the definition of a customer. However, the boards decided that it would not be feasible to develop application guidance that would apply uniformly to various industries because the nature of the relationship (ie supplier-customer versus collaboration or partnership) would depend on specific terms and conditions in those contracts. The boards observed that in many arrangements highlighted by respondents, an entity would need to consider all relevant facts and circumstances, such as the purpose of the activities undertaken by the counterparty, to determine whether the counterparty is a customer. Examples of arrangements in which an entity would need to make that assessment are as follows:

- (a) collaborative research and development efforts between biotechnology and pharmaceutical entities or similar arrangements in the aerospace and defence, technology and healthcare industries or in higher education;
- (b) arrangements in the oil and gas industry in which partners in an offshore oil and gas field may make payments to each other to settle any differences between their proportionate entitlements to production volumes from the field during a reporting period; and

- (c) arrangements in the not-for-profit industry in which an entity receives grants and sponsorship for research activity and the grantor or sponsor may specify how any output from the research activity will be used.
- BC55 The boards noted that a contract with a collaborator or a partner (for example, a joint arrangement as defined in IFRS 11 *Joint Arrangements* or a collaborative arrangement within the scope of Topic 808 *Collaborative Arrangements*) could also be within the scope of IFRS 15 if that collaborator or partner meets the definition of a customer for some or all of the terms of the arrangement.
- BC56 The boards also noted that in some cases it might be appropriate for an entity to apply the principles of IFRS 15 to some transactions with collaborators or partners. For example, an entity might consider applying IFRS 15 to a collaborative arrangement or partnership, provided such application is appropriate in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* or, for an entity applying US GAAP, provided there are not more relevant authoritative requirements in US GAAP.
- BC57 Notwithstanding the boards' decision that only contracts with customers should be accounted for under IFRS 15, the boards also decided that some of the requirements in IFRS 15 should apply to the transfer of non-financial assets that are not an output of an entity's ordinary activities (see paragraphs BC494–BC503).

Exchanges of products to facilitate a sale to another party (paragraph 5(d))

- BC58 In industries with homogeneous products, it is common for entities in the same line of business to exchange products to facilitate sales to customers or potential customers other than the parties to the exchange. For example, an oil supplier may swap inventory with another oil supplier to reduce transport costs, meet immediate inventory needs, or otherwise facilitate the sale of oil to the end customer. The boards noted that the party exchanging inventory with the entity meets the definition of a customer, because it has contracted with the entity to obtain an output of the entity's ordinary activities. Consequently, in the absence of specific requirements, an entity might recognise revenue once for the exchange of inventory and then again for the sale of the inventory to the end customer. The boards decided that this outcome would be inappropriate for the following reasons:
- (a) it would have grossed up revenues and expenses and made it difficult for users of financial statements to assess the entity's performance and gross margins during the reporting period; and
- (b) some view the counterparty in those arrangements as also acting as a supplier and not as a customer.
- BC59 The boards considered modifying the definition of a customer. However, they rejected that alternative because of concerns about unintended consequences. Consequently, the boards decided to exclude from the scope of IFRS 15 transactions involving non-monetary exchanges between entities in the same line of business to facilitate sales to customers or to potential customers. The

FASB noted such exchanges should remain within the scope of Topic 845 on non-monetary transactions.

Contracts with customers outside the scope of the requirements (paragraph 5)

BC60 The boards also excluded from the scope of IFRS 15 three types of contracts with customers that they are addressing in other Standards:

- (a) leases;
- (b) insurance contracts; and
- (c) financial instruments and other contractual rights or obligations within the scope of the boards' other Standards.

BC61 Some respondents asked the FASB to clarify what is meant by 'contractual rights or obligations' in paragraph 5 of the requirements, because those respondents stated that it is unclear whether financial instrument arrangements that are addressed elsewhere in the Codification, such as letters of credit and loan commitments (addressed in Topic 440 *Commitments*), would be included within the scope of Topic 606. The FASB noted that its intention is that if specific requirements in other Topics of the Codification deal with a transaction, the more detailed requirements from those other Topics should be applied rather than the requirements in Topic 606. For example, the FASB decided to exclude from the scope of Topic 606 guarantees (other than product warranties) that are within the scope of Topic 460 *Guarantees*, because the focus of the existing accounting requirements for those guarantee arrangements relates primarily to recognising and measuring a guarantee liability.

BC62 Some respondents reasoned that excluding some contracts with customers from the scope of IFRS 15 (such as those identified in paragraph BC60) could perpetuate the development of industry-specific or transaction-specific revenue recognition guidance, which would be inconsistent with the Revenue Recognition project's stated objective. The boards disagreed with that view. In the boards' view, IFRS 15 provides them with a framework for considering revenue issues in other standard-setting projects. The boards decided that, within the context of those other projects, a different basis of accounting for those contracts with customers might provide users of financial statements with more relevant information.

BC63 Other respondents identified what they perceived to be a contradiction within the scope requirements in IFRS 15 and IFRS 9. Those respondents stated that some of the requirements for accounting for contract assets (which would meet the definition of a financial asset) are inconsistent with the requirements in financial instruments Standards for accounting for financial assets. For example, in some cases a contract asset is not required to be adjusted for the time value of money (see paragraph BC236), and in other cases the contract asset might initially be measured at an amount that excludes some of the expected cash flows if the transaction price includes variable consideration (see paragraphs BC189–BC223). However, the IASB

disagreed with those respondents. The IASB noted that the requirements in paragraph 5 of IFRS 15 (together with paragraph 2(k) of IAS 39 *Financial Instruments: Recognition and Measurement*, which is a consequential amendment to IAS 39 added by IFRS 15) are clear that when a contract asset is within the scope of IFRS 15, it is not within the scope of IFRS 9.

Contracts partially within the scope of other Standards (paragraph 7)

- BC64 Some contracts with customers are partially within the scope of IFRS 15 and partially within the scope of other Standards (for example, a lease with a service contract). The boards decided that it would be inappropriate in those cases for an entity to account for the entire contract in accordance with one standard or another. This is because it could result in different accounting outcomes depending on whether the goods or services were sold on a stand-alone basis or together with other goods or services.
- BC65 The boards considered whether the requirements in IFRS 15 should be the default approach for separating a contract and allocating consideration to each part. However, specific issues could arise in separating contracts that are not within the scope of IFRS 15. For example, a financial instrument or an insurance contract might require an entity to provide services that are best accounted for in accordance with IFRS 9, Subtopic 942-605 *Financial Services – Depository and Lending – Revenue Recognition*, IFRS 4 *Insurance Contracts*, or Subtopic 944-605 *Financial Services – Insurance – Revenue Recognition*.
- BC66 Consequently, the boards decided that if other Standards specify how to separate and/or initially measure parts of a contract, an entity should first apply those Standards. In other words, the more specific Standard would take precedence in accounting for a part of a contract and any residual consideration should be allocated to the part(s) of the contract within the scope of IFRS 15. This rationale is consistent with the principle in IFRS 15 related to scope, which is that another Standard should be applied to a portion of the contract or arrangement if that Standard provides specific requirements for that portion of the contract or arrangement. The boards' decision is also consistent with the requirements for multiple-element arrangements in US GAAP that were replaced by Topic 606. The boards noted that this decision results in any discount in the overall arrangement being allocated to the portion of the arrangement within the scope of IFRS 15.

Identifying the contract (paragraphs 9–16)

- BC67 The boards decided that the revenue recognition model would apply to a contract with a customer only when the criteria in paragraph 9 of IFRS 15 are met. The rationale for those criteria is described in paragraphs BC33–BC46.
- BC68 IFRS 15 applies to a single contract with a customer. In many cases, the contract that is accounted for separately will be the individual contract negotiated with the customer. However, the structure and scope of a contract can vary depending on how the parties to the contract decide to record their agreement. For instance, there may be legal or commercial reasons for the

parties to use more than one contract to document the sale of related goods or services or to use a single contract to document the sale of unrelated goods or services. One of the boards' objectives in developing IFRS 15 is that the accounting for a contract should depend on an entity's present rights and obligations rather than on how the entity structures the contract.

Applying IFRS 15 at a portfolio level

BC69 IFRS 15 specifies the accounting required for an individual contract. Many entities have a large number of contracts and as a result some respondents noted practical challenges in applying the model on a contract-by-contract basis. These respondents questioned whether it would always be necessary to apply IFRS 15 on a contract-by-contract basis. The boards observed that the way in which an entity applies the model to its contracts is not a matter for which the boards should specify requirements. Nonetheless, in the light of the feedback, the boards decided to include a practical expedient in paragraph 4 of IFRS 15 to acknowledge that a practical way to apply IFRS 15 to some contracts may be to use a 'portfolio approach'. The boards acknowledged that an entity would need to apply judgement in selecting the size and composition of the portfolio in such a way that the entity reasonably expects that application of the revenue recognition model to the portfolio would not differ materially from the application of the revenue recognition model to the individual contracts or performance obligations in that portfolio. In their discussions, the boards indicated that they did not intend for an entity to quantitatively evaluate each outcome and, instead, the entity should be able to take a reasonable approach to determine the portfolios that would be appropriate for its types of contracts.

BC70 The boards observed that because it is a practical way to apply IFRS 15, the portfolio approach may be particularly useful in some industries in which an entity has a large number of similar contracts and applying the model separately for each contract may be impractical. For example, entities in the telecommunications industry explained that implementing accounting systems to determine the stand-alone selling price for the promised goods or services in each contract and, in turn, allocating the transaction price to the performance obligations identified in that contract would be complex and costly (see paragraphs BC287–BC293).

Combination of contracts (paragraph 17)

BC71 The boards decided to include requirements in paragraph 17 of IFRS 15 for when an entity should combine two or more contracts and account for them as a single contract. This is because, in some cases, the amount and timing of revenue might differ depending on whether an entity accounts for two or more contracts separately or accounts for them as one contract.

BC72 The boards decided that entering into contracts at or near the same time is a necessary condition for the contracts to be combined. That decision is consistent with the objective of identifying the contract that is to be accounted for as the unit of account because that assessment is also performed at contract inception.

- BC73 The boards decided that in addition to entering into contracts at or near the same time, the contracts should satisfy one or more of the criteria in paragraph 17 of IFRS 15 for the contracts to be combined. The boards observed that when either criterion (a) or (b) in paragraph 17 of IFRS 15 is met, the relationship between the consideration in the contracts (ie the price interdependence) is such that if those contracts were not combined, the amount of consideration allocated to the performance obligations in each contract might not faithfully depict the value of the goods or services transferred to the customer. The boards decided to include the criterion in paragraph 17(c) of IFRS 15 to avoid the possibility that an entity could effectively bypass the requirements for identifying performance obligations depending on how the entity structures its contracts.
- BC74 The boards clarified that for two or more contracts to be combined, they should be with the same customer. However, the boards acknowledged that in some situations, contracts with related parties (as defined in IAS 24 *Related Party Disclosures* and Topic 850 *Related Party Disclosures*) should be combined if there are interdependencies between the separate contracts with those related parties. Thus, in those situations, combining the contracts with related parties results in a more appropriate depiction of the amount and timing of revenue recognition.
- BC75 The boards also considered whether to specify that all contracts should be combined if they were negotiated as a package to achieve a single commercial objective, regardless of whether those contracts were entered into at or near the same time with the same customer. However, the boards decided not to do this, primarily because they were concerned that doing so could have had the unintended consequence of an entity combining too many contracts and not faithfully depicting the entity's performance. Furthermore, the boards decided that an entity should apply judgement to determine whether a contract is entered into 'at or near the same time'. However, the boards noted that the longer the period between the commitments of the parties to the contracts, the more likely it is that the economic circumstances affecting the negotiations have changed.

Contract modifications (paragraphs 18–21)

- BC76 The boards observed that previous revenue recognition requirements did not include a general framework for accounting for contract modifications. Therefore, the boards decided to include requirements regarding contract modifications in IFRS 15 to improve consistency in the accounting for contract modifications. As the revenue recognition model developed, the boards proposed different approaches to account for contract modifications. However, each approach was developed with the overall objective of faithfully depicting an entity's rights and obligations in the modified contract. The boards concluded that to faithfully depict the rights and obligations arising from a modified contract, an entity should account for some modifications prospectively and for other modifications on a cumulative catch-up basis.

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- BC77 The boards decided that a contract modification should be accounted for prospectively if the additional promised goods or services are distinct and the pricing for those goods or services reflects their stand-alone selling price (see paragraph 20 of IFRS 15). The boards decided that when those criteria are met, there is no economic difference between an entity entering into a separate contract for the additional goods or services and an entity modifying an existing contract.
- BC78 The boards also decided that a contract modification should be accounted for prospectively when the goods or services to be provided after the modification are distinct from the goods or services already provided (see paragraph 21(a) of IFRS 15). The boards decided that this should be the case regardless of whether the pricing of the additional promised goods or services reflected their stand-alone selling prices. This is because accounting for those types of modifications on a cumulative catch-up basis could be complex and may not necessarily faithfully depict the economics of the modification, because the modification is negotiated after the original contract and is based on new facts and circumstances. Therefore, this approach avoids opening up the accounting for previously satisfied performance obligations and, thus, avoids any adjustments to revenue for satisfied performance obligations.
- BC79 Some respondents were concerned that an entity would also be required to use a cumulative catch-up basis to account for modifications to a contract with a single performance obligation that is made up of a series of distinct goods or services. Those contracts typically include repetitive services, such as energy contracts or mobile phone airtime services. The boards considered those concerns and clarified in paragraph 21(a) of IFRS 15 that the determination of whether a modification is accounted for prospectively depends on whether the remaining promises in the contract are for distinct goods or services. This is the case even if an entity determines that it has a single performance obligation, provided that the performance obligation represents a series of distinct goods or services (see paragraphs BC113–BC116).
- BC80 The boards decided that if the remaining goods or services are not distinct and are part of a single performance obligation that is partially satisfied (ie a performance obligation satisfied over time), an entity should recognise the effect of the modification on a cumulative catch-up basis. This requires an entity to update the transaction price and the measure of progress towards complete satisfaction of a performance obligation, both of which may change as a result of the contract modification. That approach is particularly relevant to, and generally accepted in, the construction industry because a modification to those types of contracts would typically not result in the transfer of additional goods or services that are distinct from those promised in the existing contract.
- BC81 Respondents also asked how the requirements for contract modifications would apply to unpriced change orders (see paragraph BC39) and contract claims (ie specific modifications in which the changes in scope and price are unapproved or in dispute). IFRS and US GAAP previously included specific guidance for unpriced change orders and contract claims within construction-type and production-type contracts. The boards decided that it

was unnecessary to provide specific requirements for the accounting for these types of modifications because IFRS 15 includes the relevant requirements, specifically:

- (a) paragraphs 18 and 19 of IFRS 15 require an entity to determine whether the rights and obligations of the parties to the contract that are created or changed by the unpriced change order or contract claim are enforceable;
- (b) paragraph 19 of IFRS 15 requires an entity to estimate the change to the transaction price for the unpriced change order or contract claim; and
- (c) paragraph 21 of IFRS 15 requires an entity to determine whether the unpriced change order or contract claim should be accounted for on a prospective basis or a cumulative catch-up basis.

Interaction between changes in the transaction price and contract modifications

BC82 The 2011 Exposure Draft proposed that an entity would account for contract modifications that result only in a change in the contract price on a cumulative catch-up basis because this would be consistent with the requirements for changes in the transaction price (as a result of changes in the estimate of variable consideration). In their redeliberations, the boards noted that the proposal would result in very different accounting outcomes depending on whether a distinct good or service was included in the modification. This is because modifications that change only the price would be accounted for on a cumulative catch-up basis, whereas modifications in which a distinct good or service (no matter how small) is added to the contract at the same time as a price change would be accounted for on a prospective basis. Furthermore, the boards noted that changes in the transaction price arising from a contract modification and changes in the expectations of variable consideration are the result of different economic events—a change in the expectation of variable consideration arises from a change in a variable that was identified and agreed upon at contract inception, whereas a change in price arising from a contract modification arises from a separate and subsequent negotiation between the parties to the contract. Consequently, the boards decided that a contract modification resulting only in a change in the contract price should be accounted for in a manner that is consistent with other contract modifications.

BC83 Some respondents requested that the boards clarify how an entity should allocate a change in the transaction price that occurs after a modification of the contract (that is accounted for in accordance with paragraph 21(a) of IFRS 15) but the change in the transaction price is attributable to an amount of variable consideration promised before the modification. This may occur because the estimate of the amount of variable consideration in the initial contract has changed or is no longer constrained. Specifically, those respondents asked whether, in those circumstances, an entity should allocate the corresponding change in the transaction price to the performance obligations in the modified contract, or to the performance obligations

identified in the contract before the modification (ie the initial contract), including to performance obligations that were satisfied before the modification. In response to that feedback, the boards clarified in paragraph 90 of IFRS 15 that the allocation of the change in transaction price in those circumstances depends on whether, and the extent to which, the change in the transaction price is attributable to an amount of variable consideration promised before the modification. In providing that clarification, the boards noted that it would be appropriate in those circumstances to allocate a change in the transaction price to the performance obligations identified in the initial contract, if the promised variable consideration and the resolution of the uncertainty associated with that amount of variable consideration are not affected by the contract modification.

Identifying performance obligations

Definition of a performance obligation (Appendix A)

- BC84 IFRS 15 distinguishes between obligations to provide goods or services to a customer and other obligations by defining those obligations to provide goods or services as performance obligations. The notion of a performance obligation is similar to the notions of deliverables, components or elements of a contract in previous revenue Standards. Although the notion of a performance obligation is implicit in previous revenue Standards, the term ‘performance obligation’ has not been defined previously.
- BC85 The boards’ objective in developing the definition of a performance obligation was to ensure that entities appropriately identify the unit of account for the goods and services promised in a contract with a customer. The boards decided that because the revenue recognition model is an allocated transaction price model, identifying a meaningful unit of account that depicts the goods and services in the contract is fundamental for the purpose of recognising revenue on a basis that faithfully depicts the entity’s performance in transferring the promised goods or services to the customer.
- BC86 The boards decided that a performance obligation could be either of the following:
- (a) a good or service (or a bundle of goods or services) that is distinct (see paragraphs BC94–BC112); or
 - (b) a series of distinct goods or services that are substantially the same and have the same pattern of transfer (see paragraphs BC113–BC116).

Identifying the promised goods or services (paragraphs 24–25)

- BC87 Before an entity can identify its performance obligations in a contract with a customer, the entity would first need to identify all of the promised goods or services in that contract. The boards noted that in many cases, all of the promised goods or services in a contract might be identified explicitly in that

contract. However, in other cases, promises to provide goods or services might be implied by the entity's customary business practices. The boards decided that such implied promises should be considered when determining the entity's performance obligations, if those practices create a valid expectation of the customer that the entity will transfer a good or service (for example, some when-and-if-available software upgrades). The boards also noted that the implied promises in the contract do not need to be enforceable by law. If the customer has a valid expectation, then the customer would view those promises as part of the negotiated exchange (ie goods or services that the customer expects to receive and for which it has paid). The boards noted that in the absence of these requirements developed by the boards, an entity might recognise all of the consideration in a contract as revenue even though the entity continues to have remaining (implicit) promises related to the contract with the customer.

- BC88 Some respondents suggested that some promised goods or services should be excluded from the scope of IFRS 15 and accounted for as marketing expenses or incidental obligations, even though those promises would meet the definition of a performance obligation. Examples of such promised goods or services may include 'free' handsets provided by telecommunication entities, 'free' maintenance provided by automotive manufacturers and customer loyalty points awarded by supermarkets, airlines and hotels. Those respondents stated that revenue should be recognised only for the main goods or services for which the customer has contracted and not for what they consider to be marketing incentives and other incidental obligations.
- BC89 The boards observed that when a customer contracts with an entity for a bundle of goods or services, it can be difficult and subjective for the entity to identify the main goods or services for which the customer has contracted. In addition, the outcome of that assessment could vary significantly depending on whether the entity performs the assessment from the perspective of its business model or from the perspective of the customer. Consequently, the boards decided that all goods or services promised to a customer as a result of a contract give rise to performance obligations because those promises were made as part of the negotiated exchange between the entity and its customer. Although the entity might consider those goods or services to be marketing incentives or incidental goods or services, they are goods or services for which the customer pays and to which the entity should allocate consideration for purposes of revenue recognition. However, the boards observed that in some cases, an entity might provide incentives to a customer that would not represent a performance obligation if those incentives are provided independently of the contract that they are designed to secure. (See paragraphs BC386–BC395 for additional discussion on marketing incentives and the accounting for customer options to acquire additional goods or services.)

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- BC90 For similar reasons, the boards decided not to exempt an entity from accounting for performance obligations that the entity might regard as being perfunctory or inconsequential.³ Instead, an entity should assess whether those performance obligations are immaterial to its financial statements as described in IAS 8 and FASB Concepts Statement No. 8 *Conceptual Framework for Financial Reporting*.
- BC91 To help an entity identify the promised goods or services, IFRS 15 provides examples of the types of promises that can represent goods or services to the customer. In response to feedback received, the boards clarified that the following can also represent promised goods or services:
- (a) providing a service of standing ready or making goods or services available (see paragraph BC160); and
 - (b) granting rights to goods or services to be provided in the future (see paragraph BC92).
- BC92 The boards observed that it was important to clarify that granting a right to goods or services to be provided in the future, such as when an entity makes a promise to provide goods or services to its customer's customer, would give rise to performance obligations for the entity. Those types of promises exist in distribution networks in various industries but are particularly common in the automotive industry. For example, when a manufacturer sells a motor vehicle to its customer (a dealer), the manufacturer may also promise to provide additional goods or services (such as maintenance) to the dealer's customer. IFRS 15 requires an entity to identify all of the promises—both explicit and implicit—that are made to the customer as part of the contract with that customer. Consequently, a promise of a good or service (such as maintenance) that the customer can pass on to its customer would be a performance obligation if the promise could be identified (explicitly or implicitly) in the contract with the customer. However, the boards noted that some promised goods or services might not represent performance obligations if those promises did not exist (explicitly or implicitly) at the time that the parties agreed to the contract.
- BC93 The boards also clarified that an entity should not account for activities it may perform that do not transfer goods or services to the customer. This may occur in many contracts in which an entity undertakes separate activities that do not directly transfer goods or services to the customer (for example, service contracts that require significant setup costs), even though those activities are required to successfully transfer the goods or services for which the customer has contracted. The boards decided that including those activities as performance obligations would have been inconsistent with the core revenue recognition principle because those activities do not result in a transfer of goods or services to the customer.

³ The FASB subsequently decided to amend Topic 606 to state that an entity is not required to assess whether promised goods or services are performance obligations if they are immaterial within the context of the contract with the customer. The IASB's considerations for deciding not to make similar amendments to IFRS 15 are explained in paragraphs BC116A–BC116E.

Identifying when promises represent performance obligations (paragraphs 22–30)

- BC94 Contracts with customers can include many promises to transfer goods or services. In the Discussion Paper, the boards proposed that an entity should review the timing of the transfer of the promised goods or services to identify the performance obligations that it should account for separately. Respondents to the Discussion Paper were concerned that this proposal would have required an entity to account separately for every promised good or service in a contract that is transferred at a different time, which would not be practical for many contracts, especially for long-term service and construction contracts. Consequently, the boards decided to provide clearer requirements that result in an entity identifying performance obligations in a way that is practical and results in a pattern of revenue recognition that faithfully depicts the transfer of goods or services to the customer.
- BC95 In developing those requirements, the boards observed that in many contracts, identifying the promised goods or services that an entity should account for separately is straightforward. Consequently, the boards developed a principle for identifying performance obligations that separates promised goods or services in a relevant way when applied across the various industries and transactions within the scope of IFRS 15. That principle is the notion of a distinct good or service. The term ‘distinct’, in an ordinary sense, suggests something that is different, separate or dissimilar. A majority of respondents agreed with using the principle of distinct goods or services to identify the performance obligations in a contract. However, many asked the boards to refine and further clarify the requirements for determining when a good or service is distinct.
- BC96 Consequently, the boards decided that for a good or service to be distinct, the criteria in paragraph 27 of IFRS 15 must be met. The boards’ deliberations of those criteria are discussed in the following sections.

Capable of being distinct

- BC97 The boards decided that a good or service must possess some specified minimum characteristics to be accounted for separately. Specifically, the good or service must be capable of being distinct—that is, the good or service is capable of providing a benefit to the customer either on its own or together with other resources that are readily available to the customer. The boards were concerned that requiring an entity to account separately (and estimate a stand-alone selling price) for a good or service that is not capable of providing a benefit to the customer might result in information that would not be relevant to users of financial statements. For example, if an entity transferred a machine to the customer, but the machine is only capable of providing a benefit to the customer after an installation process that only the entity can provide, the machine would not be distinct.
- BC98 The 2010 Exposure Draft addressed this notion of a minimum characteristic by proposing that a good or service should have a distinct function—that is, the good or service should have utility either on its own or together with other goods or services that the customer has acquired from the entity or that

are sold separately by the entity or another entity. Respondents requested additional guidance on the meaning of ‘distinct function’ because they considered that almost any element of a contract could have utility in combination with other goods or services.

- BC99 Consequently, the boards refined the notion of distinct function and developed the criterion in paragraph 27(a) of IFRS 15. In addition, the boards included the requirements in paragraph 28 of IFRS 15 (which were derived from the Basis for Conclusions on the 2011 Exposure Draft) to help an entity apply that criterion and assess whether a customer can benefit from the good or service on its own or together with other resources. Those requirements focus on the notion of economic benefits, which many respondents explained was helpful in assessing whether the customer can benefit from the good or service on its own or together with other resources. The boards noted that, conceptually, any good or service that is regularly sold separately should be able to be used on its own or with other resources. Otherwise, there would be no market for an entity to provide that good or service on a stand-alone basis.
- BC100 The boards observed that the assessment of whether the ‘customer can benefit from the goods or services on its own’ should be based on the characteristics of the goods or services themselves instead of the way in which the customer may use the goods or services. Consequently, an entity would disregard any contractual limitations that might preclude the customer from obtaining readily available resources from a source other than the entity.
- BC101 The attributes of a distinct good or service are comparable to previous revenue recognition requirements for identifying separate deliverables in a multiple-element arrangement, which specified that a delivered item must have ‘value to the customer on a stand-alone basis’ for an entity to account for that item separately. However, the boards decided against using that terminology to avoid the implication that an entity must assess the customer’s intended use for the promised goods or services in identifying the performance obligations in a contract. The boards observed that it would be difficult, if not impossible, for an entity to know the customer’s intentions in a given contract.

Distinct within the context of the contract⁴

- BC102 In some cases, even though the individual goods or services promised as a bundle of goods or services might be capable of being distinct, those goods or services should not be accounted for separately because it would not result in a faithful depiction of the entity’s performance in that contract. As an example, many construction-type and production-type contracts involve transferring to the customer many goods and services that are capable of being distinct (such as various building materials, labour and project

⁴ *Clarifications to IFRS 15* issued in April 2016 amended paragraphs 27 and 29 of IFRS 15 to clarify that the objective of assessing whether an entity’s promises to transfer goods or services to the customer are separately identifiable is to determine whether the entity’s promise is to transfer (a) each of those goods or services; or (b) a combined item or items to which the promised goods or services are inputs. Amendments were also made to the factors in paragraph 29 to more clearly align them with the revised ‘separately identifiable’ principle. Paragraphs BC102–BC112 should therefore be read together with paragraphs BC116F–BC116Q, which explain the boards’ considerations in making these amendments.

management services). However, identifying all of those individual goods and services as separate performance obligations would be impractical and, more importantly, it would neither faithfully represent the nature of the entity's promise to the customer nor result in a useful depiction of the entity's performance. This is because it would result in an entity recognising and measuring revenue when the materials and other inputs to the construction or production process are provided, instead of recognising and measuring revenue when the entity performs (and uses those inputs) in the construction or production of the item (or items) for which the customer has contracted. Consequently, the boards decided that, when identifying whether goods or services are distinct, an entity should not only consider the characteristics of an individual good or service (see paragraph 27(a) of IFRS 15) but should also consider whether the promise to transfer the good or service is separately identifiable (ie distinct within the context of the contract, see paragraph 27(b) of IFRS 15).

- BC103 During the development of IFRS 15, the existence of 'separable risks' was identified as a basis for assessing whether a good or service is distinct within the context of the contract. In that assessment, the individual goods or services in a bundle would not be distinct if the risk that an entity assumes to fulfil its obligation to transfer one of those promised goods or services to the customer is a risk that is inseparable from the risk relating to the transfer of the other promised goods or services in that bundle. The boards considered whether to specify 'separable risks' as a necessary attribute of a distinct good or service. However, the boards decided that the concept of 'separable risks' may not be a practical criterion for determining whether a good or service is distinct.
- BC104 To make the notion of separable risks more operable, the boards considered other approaches for articulating the notion. However, the boards rejected those approaches for the following reasons:
- (a) distinct profit margin—in some cases, entities may decide to assign the same margin to various goods or services, even though those goods or services use different resources and are subject to different risks. In addition, for some goods or services, especially software and other types of intellectual property, cost is not a significant factor in determining price and, therefore, margins could be highly variable because they may be determined by the customer's ability to pay or to obtain substitute goods or services from another entity.
 - (b) criteria based on the notions of goods or services that are significantly modified or customised, and highly interrelated goods or services that require an entity to provide a significant service of integrating those goods or services—respondents explained that while these are relevant factors to consider to determine whether a good or service is distinct, expressing those factors as criteria could be too restrictive because they could force bundling or unbundling that did not reflect the economics of the arrangement.

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BC105 Consequently, the boards decided to specify in paragraph 27(b) of IFRS 15 that the objective in identifying whether a promised good or service is distinct within the context of the contract is to determine whether an entity's promise to transfer that good or service is separately identifiable from other promises in the contract. The notion of 'separately identifiable' is based on the notion of separable risks in paragraph BC103 (ie whether the risk that an entity assumes to fulfil its obligation to transfer one of those promised goods or services to the customer is a risk that is inseparable from the risk relating to the transfer of the other promised goods or services). The boards observed that determining whether the entity's promise to transfer a good or service is separately identifiable requires judgement, taking into account all of the facts and circumstances. The boards decided to assist entities in making that judgement by including the factors in paragraph 29 of IFRS 15.

BC106 The boards observed that the factors in paragraph 29 of IFRS 15 are not mutually exclusive. On the contrary, because the factors are based on the same underlying principle of inseparable risks, the boards noted that in many cases more than one of the factors might apply to a contract with a customer. However, each factor was developed because it may be more applicable for particular contracts or industries. The rationale for each factor is discussed in paragraphs BC107–BC112.

Significant integration service (paragraph 29(a))

BC107 In circumstances in which an entity provides an integration service, the risk of transferring individual goods or services is inseparable, because a substantial part of the entity's promise to a customer is to ensure the individual goods or services are incorporated into the combined output. Thus, the individual goods or services are inputs to produce a single output. The boards observed that this factor may be relevant in many construction contracts in which the contractor provides an integration (or contract management) service to manage and co-ordinate the various construction tasks and to assume the risks associated with the integration of those tasks. Moreover, the integration service will require a contractor to co-ordinate the tasks performed by any subcontractors and ensure that those tasks are performed in accordance with the contract specifications, thus ensuring the individual goods or services are appropriately incorporated into the combined item for which the customer has contracted.

BC108 The boards observed that this factor could apply to industries other than the construction industry. For example, some software development contracts with significant integration services will similarly have promised goods and services that meet the criterion in paragraph 27(b) of IFRS 15. However, the boards did not intend for this factor to be applied too broadly to software integration services for which the risk that the entity assumes in integrating the promised goods or services is negligible (for example, a simple installation of software that does not require significant modification). Therefore, to provide some additional clarification for many software-type contracts, the boards included the factor in paragraph 29(b) of IFRS 15.

Significant modification or customisation (paragraph 29(b))

- BC109 In some industries, such as the software industry, the notion of inseparable risks is more clearly illustrated by assessing whether one good or service significantly modifies or customises another good or service. This is because if a good or service modifies or customises another good or service in the contract, each good or service is being assembled together (ie as inputs) to produce a combined output for which the customer has contracted.
- BC110 For example, an entity may promise to provide a customer with existing software and also promise to customise that software so that it will function with the customer's existing infrastructure such that the entity is providing the customer with a fully integrated system. In this case, if the customisation service requires the entity to significantly modify the existing software in such a way that the risks of providing the software and the customisation service are inseparable, the entity may conclude that the promises to transfer the software and the customisation service would not be separately identifiable and, therefore, those goods or services would not be distinct within the context of the contract.

Highly dependent or highly interrelated (paragraph 29(c))

- BC111 The boards decided to include the factor in paragraph 29(c) of IFRS 15 because, in some cases, it might be unclear whether the entity is providing an integration service (see paragraph 29(a)) or whether the goods or services are significantly modified or customised (see paragraph 29(b)). However, the individual goods and services in the contract may still not be separately identifiable from the other goods or services promised in the contract. This may be because the goods or services are highly dependent on, or highly interrelated with, other promised goods or services in the contract in such a way that the customer could not choose to purchase one good or service without significantly affecting the other promised goods or services in the contract.
- BC112 Consider the following example—an entity agrees to design an experimental new product for a customer and to manufacture 10 prototype units of that product. The specifications for the product include functionality that has yet to be proved. Consequently, the entity will be required to continue to revise the design of the product during the construction and testing of the prototypes and make any necessary modifications to in-progress or completed prototypes. The entity expects that most or all of the units to be produced may require some rework because of design changes made during the production process. In that case, the customer may not be able to choose whether to purchase only the design service or the manufacturing service without significantly affecting one or the other. This is because the risk of providing the design service is inseparable from the manufacturing service. Thus, although each promise may have benefit on its own, within the context of the contract, they are not separately identifiable. This is because the entity determines that each promise is highly dependent on, and highly interrelated with, the other promises in the contract.

A series of distinct goods or services that are substantially the same and have the same pattern of transfer (paragraph 22(b))

- BC113 The boards decided to specify that 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 customer would be a single performance obligation if two criteria are met. The boards decided to include this notion as part of the definition of a performance obligation to simplify the application of the model and to promote consistency in the identification of performance obligations in circumstances in which the entity provides the same good or service consecutively over a period of time (for example, a repetitive service arrangement). To be accounted for as a single performance obligation, each of those promised goods or services must be performance obligations satisfied over time in accordance with paragraph 35 of IFRS 15.
- BC114 The boards observed that without this part of the definition, applying the model might present some operational challenges when an entity provides a series of distinct goods or services that are substantially the same. Otherwise, the entity would be required to identify multiple distinct goods or services, allocate the transaction price to each of the resulting performance obligations on a stand-alone selling price basis and then recognise revenue when those performance obligations are satisfied. For example, in a repetitive service contract such as a cleaning contract, transaction processing or a contract to deliver electricity, an entity would be required to allocate the overall consideration to each increment of service (for example, each hour of cleaning) to be provided in the contract. The boards decided that it would not be cost-effective to apply the model in this manner and determined that including paragraph 22(b) of IFRS 15 as part of the definition of a performance obligation would alleviate costs. This is because when paragraph 22(b) of IFRS 15 applies (ie the contract includes a promise to transfer a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer), an entity will identify a single performance obligation and allocate the transaction price to the performance obligation. The entity will then recognise revenue by applying a single measure of progress to that performance obligation.
- BC115 The boards noted that if an entity determines it has a performance obligation that meets the criterion in paragraph 22(b) of IFRS 15, an entity should consider the distinct goods or services in the contract, rather than the performance obligation, for the purposes of contract modifications and the allocation of variable consideration.
- BC116 In their redeliberations, the boards observed that paragraph 22(b) of IFRS 15 applies to goods or services that are delivered consecutively, rather than concurrently. The boards noted that IFRS 15 would not need to specify the accounting for concurrently delivered distinct goods or services that have the same pattern of transfer. This is because, in those cases, an entity is not precluded from accounting for the goods or services as if they were a single performance obligation, if the outcome is the same as accounting for the goods and services as individual performance obligations.

Clarifications to IFRS 15 (amendments issued in April 2016)**Promised goods or services that are immaterial within the context of the contract**

- BC116A The TRG discussed an implementation question about whether an entity should identify items or activities as promised goods or services that were not identified as deliverables or components under previous revenue Standards. A specific concern was raised about the boards' decision (see paragraph BC90) not to exempt an entity from accounting for performance obligations that the entity might regard as being perfunctory or inconsequential. Some stakeholders held the view that IFRS 15 might require an entity to identify significantly more performance obligations than would have been the case under previous revenue Standards.
- BC116B In response to stakeholders' concerns, the FASB decided to amend Topic 606 to state that an entity is not required to assess whether promised goods or services are performance obligations if they are immaterial within the context of the contract with the customer. The FASB decided to specify that an entity is required to consider whether a promised good or service is material only at the contract level because it would be unduly burdensome to require an entity to aggregate and determine the effect on its financial statements of those items or activities determined to be immaterial at the contract level. In addition, the FASB decided to specify that an entity is required to accrue the costs, if any, to transfer immaterial goods or services to the customer in instances in which the costs will be incurred after the satisfaction of the performance obligation (and recognition of revenue) to which those immaterial goods or services relate.
- BC116C Having considered the wider implications of amending IFRS 15, the IASB decided that it was not necessary to incorporate similar wording into IFRS 15. The TRG's discussion highlighted that the concerns raised primarily related to potential changes to practice under US GAAP. Previous revenue Standards under IFRS did not contain similar language to the guidance issued by the staff of the US Securities and Exchange Commission on inconsequential or perfunctory performance obligations. The TRG's discussion also indicated that IFRS stakeholders can understand and apply the requirements of IFRS 15 in this area.
- BC116D In its deliberations, the IASB expressed the view that the concerns raised relate to the application of materiality concepts rather than the application of the requirements in IFRS 15. As described in paragraph BC84, the boards intended the notion of a performance obligation to be similar to the notions of deliverables, components or elements of a contract in previous revenue Standards. The IASB noted that IFRS 15 requires an entity to identify performance obligations rather than promised goods or services. Accordingly, although an entity makes an assessment of the goods or services promised in a contract in order to identify material performance obligations, the boards did not intend to require an entity to individually identify every possible promised good or service.

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BC116E In reaching its decision, the IASB also observed that the explanation in paragraph BC90 should be read within the context of the boards' explanation of the development of IFRS 15 rather than as implying that an entity is required to identify perfunctory or inconsequential goods or services promised in a contract. One of the reasons that the IASB decided not to introduce an exemption for perfunctory or inconsequential performance obligations is that it was not considered necessary, both because of how the concept of 'distinct' is applied and also because of the application of materiality. In assessing promised goods or services and identifying performance obligations, entities should consider not only materiality considerations but also the overall objective of IFRS 15. The IASB further noted that materiality is an overarching concept that applies throughout IFRS and not just when it is mentioned explicitly.

Identifying performance obligations (paragraphs 27–30)

BC116F The TRG discussed issues relating to the principle in paragraph 27(b) regarding when a promised good or service is separately identifiable (ie distinct within the context of a contract) and the supporting factors in paragraph 29. The discussion informed the boards about potential diversity in stakeholders' understanding and indicated that there was a risk of paragraph 29(c) being applied more broadly than intended, resulting in promised goods or services being inappropriately combined and accounted for as a single performance obligation. Stakeholders asked about the application of this factor to scenarios in which one of the promised goods or services is dependent on the transfer of the other, such as a contract for equipment and related consumables that are required for the equipment to function. Some stakeholders suggested that, although the promised goods or services may be capable of being distinct, if one of the goods or services was dependent on the other, the promised goods or services would not be distinct within the context of the contract.

BC116G In the light of the TRG discussions, the IASB was initially of the view that the discussions highlighted educational needs and that, given the nature of the issues raised, amendments to IFRS 15 were not required and that the examples accompanying IFRS 15 could be clarified to illustrate the application of the requirements. Consequently, in its Exposure Draft *Clarifications to IFRS 15*, the IASB proposed to add some new examples, and to amend some of the existing examples that accompany IFRS 15. The FASB decided to propose amendments to Topic 606 to clarify the guidance relating to the identification of performance obligations. In particular, their proposed amendments included expanding the articulation of the 'separately identifiable' principle and reframing the existing factors in paragraph 606-10-25-21 (paragraph 29 of IFRS 15) to align them with the amended principle.

BC116H Some respondents to the IASB's Exposure Draft asked for the amendments proposed by the FASB to be incorporated into paragraph 29 of IFRS 15. They expressed concerns about differences in wording between IFRS and US GAAP and also indicated that the FASB's proposed amendments would improve the understanding of the separately identifiable principle and the operability of the requirements. Step 2 is a fundamental part of IFRS 15 that affects accounting in subsequent steps of the revenue recognition model.

Consequently, in its redeliberations of the amendments the IASB concluded that the benefits of retaining converged requirements on this topic outweigh the potential costs of amending the requirements. Accordingly, the IASB decided to amend IFRS 15 to clarify the principle and the factors that indicate when two or more promises to transfer goods or services are not separately identifiable. Those amendments are the same as the FASB's related amendments to Topic 606.

- BC116I Although the wording describing the separately identifiable principle in paragraph 29 has been amended, the amendments clarify the boards' intentions and are not a change to the underlying principle. The boards observed that applying the principle in paragraph 27(b) requires judgement, taking into account facts and circumstances (see paragraph BC105). Even after amending the factors in paragraph 29 of IFRS 15, the boards recognise that judgement will be needed to determine whether promised goods or services are distinct within the context of the contract.
- BC116J The amendments are intended to convey that an entity should evaluate whether its promise, within the context of the contract, is to transfer each good or service individually or a combined item (or items) that comprises the individual goods or services promised in the contract. Therefore, entities should evaluate whether the promised goods or services in the contract are outputs or, instead, are inputs to a combined item (or items). In many cases, the inputs to a combined item concept might be further explained as a situation in which an entity's promise to transfer goods or services results in a combined item that is more than (or substantively different from) the sum of those individual promised goods and services. For example, in a contract to build a wall, the promise to provide bricks and the promise to provide labour are not separately identifiable from each other within the context of the contract because those promises together comprise the promise to the customer to build the wall.
- BC116K The boards previously considered the concept of 'separable risks' (see paragraph BC103) as an alternative basis for assessing whether an entity's promise to transfer a good or service is separately identifiable from other promises in the contract. Although the boards decided not to use this terminology in IFRS 15, the notion of separable risks continues to influence the separately identifiable principle. The evaluation of whether an entity's promise is separately identifiable considers the relationship between the various goods or services within the contract in the context of the process of fulfilling the contract. Therefore, an entity should consider the level of integration, interrelation or interdependence among the promises to transfer goods or services. The boards observed that rather than considering whether one item, by its nature, depends on the other (ie whether two items have a functional relationship), an entity evaluates whether there is a transformative relationship between the two items in the process of fulfilling the contract.
- BC116L The boards decided to reframe the factors in paragraph 29 of IFRS 15 to more clearly align them with the revised wording of the separately identifiable principle. This clarification emphasises that the separately identifiable principle is applied within the context of the bundle of promised goods or

services in the contract rather than within the context of each individual promised good or service. The separately identifiable principle is intended to identify when an entity's performance in transferring a bundle of goods or services in a contract is fulfilling a single promise to a customer. Accordingly, the boards revised the wording to emphasise that an entity should evaluate whether two or more promised goods or services each significantly affect the other (and, therefore, are highly interdependent or highly interrelated) in the contract. Furthermore, the boards concluded that it may be clearer to structure those factors to identify when the promises in a bundle of promised goods or services are *not* separately identifiable and, therefore, constitute a single performance obligation.

- BC116M In addition to reframing the factors in the context of a bundle of goods or services, the boards amended the factor relating to a significant integration service in paragraph 29(a) of IFRS 15 to clarify two related issues—that application of this factor is not limited to circumstances that result in a single output, and that a combined output may include more than one phase, element or unit. This concept is illustrated by the example in paragraph BC112, in which an entity agrees to design an experimental product for a customer and to manufacture 10 prototype units of that product. In the example, the design and production of the units is an iterative process and the significant integration service provided by the entity relates to all 10 prototype units.
- BC116N The TRG's discussions also highlighted that some stakeholders may have been interpreting the factors supporting paragraph 27(b) as a series of criteria. Paragraph 29, where the factors are set out, provides a non-exhaustive list of factors to consider; not all of those factors need to exist (or not exist) to conclude that the entity's promises to transfer goods or services are not (are) separately identifiable. Similarly, the boards also noted that the factors are not intended to be criteria that are evaluated independently of the separately identifiable principle. Given the wide variety of revenue arrangements that are within the scope of IFRS 15, the boards expect that there will be some instances for which the factors will be less relevant to the evaluation of the separately identifiable principle. Consequently, entities should consider the objective of the principle, not just the factors provided in paragraph 29 of IFRS 15.
- BC116O Stakeholders also asked about the effect of contractual restrictions on the identification of performance obligations. Accordingly, one of the examples added (Case D of Example 11) illustrates the boards' observation in paragraph BC100 of IFRS 15 that an entity should focus on the characteristics of the promised goods or services themselves instead of on the way in which the customer might be required to use the goods or services.
- BC116P The IASB decided that it was not necessary to add some of the examples that the FASB included in its amendments to Topic 606. In particular, the IASB concluded that an example relating to whether an anti-virus software licence is distinct from when-and-if-available updates to the software during the licence period (Example 10, Case C in Topic 606) was unnecessary. The IASB thought that this additional example was not required because Example 55

that accompanies IFRS 15 illustrates the application of the requirements on identifying performance obligations to a similar fact pattern.

- BC116Q Respondents to the Exposure Draft expressed concern that the proposed Example 10, Case B may imply that any contract manufacturing or similar arrangement would be a single performance obligation comprising goods that are not distinct. There are some similarities between the fact pattern in the example and other contracts with customers that involve project management, the production of customised goods or the manufacture of a series of identical goods. However, an entity should evaluate the nature of its promise(s) to a customer within the context of the contract. Example 10, Case B illustrates a scenario in which the entity is contractually required to undertake a significant effort to establish a customised production process specifically in order to produce the highly complex, specialised devices for which the customer has contracted. As a result, the entity's promise is to establish and provide a service of producing the contracted devices based on the customer's specifications. In contrast, other manufacturing scenarios may involve the development of a production process that can be used to produce goods for multiple contracts with the same or additional customers. In that case, the contract may not include a promise to establish a customised production process.

Shipping and handling activities

- BC116R Some stakeholders in the United States expressed differing views about when shipping and handling activities that occur after the transfer of control to the customer should be accounted for as a promised service or as a fulfilment activity. Under previous revenue Standards, entities often did not account for shipping provided in conjunction with the sale of their goods as an additional service. As a result, some stakeholders raised cost-benefit concerns and asked whether relief should be provided in respect of shipping and handling activities from the general requirement to assess the goods or services promised in a contract with a customer in order to identify performance obligations.
- BC116S When the boards discussed these concerns, board members noted that shipping and handling activities that occur before the customer obtains control of the related good are fulfilment activities. However, if control of a good has been transferred to a customer, shipping and handling services are provided in relation to the customer's good, which may indicate that the entity is providing a service to the customer.
- BC116T In response to the cost-benefit concerns raised by stakeholders, the FASB decided to amend Topic 606 to:
- (a) permit an entity, as an accounting policy election, to account for shipping and handling activities that occur after the customer has obtained control of a good as fulfilment activities; and
 - (b) explicitly state that shipping and handling activities that occur before the customer obtains control of the related good are fulfilment activities.

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BC116U Having considered the wider implications of amending IFRS 15, the IASB decided not to make a similar amendment, for the following reasons:

- (a) An accounting policy choice for shipping and handling activities after control of goods has been transferred to the customer would create an exception to the revenue recognition model and potentially reduce comparability between entities. Paragraph 22 of IFRS 15 requires an entity to assess the goods or services promised in a contract with a customer in order to identify performance obligations. The introduction of a policy choice would override this requirement.
- (b) In addition, a policy choice is applicable to all entities. Consequently, it is possible that entities with significant shipping operations would make different policy elections. This would make it more difficult for users of financial statements to understand and compare the revenue reported by different entities, including those within the same industry.

The IASB acknowledged that, because the policy choice is not available in IFRS 15, this gives rise to a difference between IFRS 15 and Topic 606.

Satisfaction of performance obligations (paragraphs 31–45)

BC117 Revenue is recognised when (or as) goods or services are transferred to a customer. This is because an entity satisfies its performance obligation by transferring control of the promised good or service underlying that performance obligation to the customer. Consequently, assessing when control of a good or service is transferred is a critical step in applying IFRS 15.

Control

BC118 Most previous revenue Standards required an entity to assess the transfer of a good or service by considering the transfer of risks and rewards of ownership. However, the boards decided that an entity should assess the transfer of a good or service by considering when the customer obtains control of that good or service, for the following reasons:

- (a) Both goods and services are assets that a customer acquires (even if many services are not recognised as an asset because those services are simultaneously received and consumed by the customer), and the boards' existing definitions of an asset use control to determine when an asset is recognised or derecognised.
- (b) Assessing the transfer of goods or services using control should result in more consistent decisions about when goods or services are transferred, because it can be difficult for an entity 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.

- (c) A risks-and-rewards approach could conflict with identifying performance obligations. For example, if an entity transfers a product to a customer but retains some risks associated with that product, an assessment based on risks and rewards might result in the entity identifying a single performance obligation that could be satisfied (and therefore revenue would be recognised) only after all the risks are eliminated. However, an assessment based on control might appropriately identify two performance obligations—one for the product and another for a remaining service, such as a fixed price maintenance agreement. Those performance obligations would be satisfied at different times.

BC119 Many respondents to both the 2010 and the 2011 Exposure Drafts agreed with using control to determine when a good or service is transferred to a customer. However, some respondents indicated that the transfer of the risks and rewards of ownership is sometimes a helpful indicator that control has transferred (see paragraph BC154).

Developing the notion of control

BC120 The boards' description of control is based on the meaning of control in the definitions of an asset in the boards' respective conceptual frameworks. Thus, the boards determined that control of a promised good or service (ie an asset) is the customer's ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. The components that make up the description of control are explained as follows:

- (a) ability—a customer must have the present right to direct the use of, and obtain substantially all of the remaining benefits from, an asset for an entity to recognise revenue. For example, in a contract that requires a manufacturer to produce an asset for a particular customer, it might be clear that the customer will ultimately have the right to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, the entity should not recognise revenue until the customer has actually obtained that right (which, depending on the contract, might occur during production or afterwards).
- (b) direct the use of—a customer's ability to direct the use of an asset refers to the customer's right to deploy that asset in its activities, to allow another entity to deploy that asset in its activities, or to restrict another entity from deploying that asset.
- (c) obtain the benefits from—the customer must have the ability to obtain substantially all of the remaining benefits from an asset for the customer to obtain control of it. Conceptually, the benefits from a good or service are potential cash flows (either an increase in cash inflows or a decrease in cash outflows). A customer can obtain the benefits directly or indirectly in many ways, such as by using, consuming, disposing of, selling, exchanging, pledging or holding an asset.

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BC121 The boards observed that the assessment of when control has transferred could be applied from the perspective of either the entity selling the good or service or the customer purchasing the good or service. Consequently, revenue could be recognised when the seller surrenders control of a good or service or when the customer obtains control of that good or service. Although in many cases both perspectives lead to the same result, the boards decided that control should be assessed primarily from the perspective of the customer. That perspective minimises the risk of an entity recognising revenue from undertaking activities that do not coincide with the transfer of goods or services to the customer.

Applying the notion of control

BC122 As described in paragraph BC119, many respondents agreed with using control as the basis for assessing when the transfer of a promised good or service (ie an asset) occurs. However, most respondents to the 2010 Exposure Draft explained that the definition was most helpful when applied to performance obligations for the transfer of goods. They commented that applying the concept of control is straightforward in those cases because, typically, it is clear that an asset has transferred from the entity to its customer. They noted, however, that the requirements were more difficult to apply to performance obligations for services and construction-type contracts, because it could be difficult to determine when a customer obtains control of a service. This is because in many service contracts the service asset is simultaneously created and consumed and, therefore, is never recognised as an asset by the customer. Even in the case of a construction contract in which there is a recognisable asset, it can be difficult to assess whether a customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, a partially completed asset that the seller is creating. Consequently, many respondents in the construction industry were concerned that they would be required to change their revenue recognition policy from using a percentage-of-completion method to a completed contract method (ie on the basis that the transfer of assets occurs only upon transfer of legal title or physical possession of the finished asset, which typically occurs upon contract completion). Those respondents explained that the outcome of applying the completed contract method to their contracts with customers would not be a faithful depiction of the economics of those contracts.

BC123 As a result, some respondents suggested that the boards provide guidance for the transfer of control of services separately from the guidance for goods. However, the boards observed that it would be difficult to clearly define a service and not all contracts that are commonly regarded as services result in a transfer of resources to customers over time. Furthermore, the boards decided that the notion of control should apply equally to both goods and services. Consequently, to address respondents' concerns, the boards decided to specify requirements that focus on the attribute of the timing of when a performance obligation is satisfied (ie when a good or service is transferred to a customer). Accordingly, IFRS 15 includes criteria for determining whether a performance obligation is satisfied over time. Those criteria are explained in the following paragraphs.

**Performance obligations satisfied over time
(paragraphs 35–37)**

BC124 The boards developed the criteria in paragraph 35 of IFRS 15 to provide an objective basis for assessing when control transfers over time and, thus, when a performance obligation is satisfied over time.

**Customer simultaneously receives and consumes benefits as
entity performs (paragraph 35(a))**

BC125 In many typical service contracts, the entity's performance creates an asset only momentarily, because that asset is simultaneously received and consumed by the customer. In those cases, the simultaneous receipt and consumption of the asset that has been created means that the customer obtains control of the entity's output as the entity performs and, thus, the entity's performance obligation is satisfied over time. For example, consider an entity that promises to process transactions on behalf of a customer. The customer simultaneously receives and consumes a benefit as each transaction is processed.

BC126 The boards observed that there may be service-type contracts in which it is unclear whether the customer receives and consumes the benefit of the entity's performance over time. This is because the notion of 'benefit' can be subjective. Consider, for example, a freight logistics contract in which the entity has agreed to transport goods from Vancouver to New York City. Many respondents suggested that the customer receives no benefit from the entity's performance until the goods are delivered to New York City. However, the boards observed that the customer does benefit from the entity's performance as it occurs because if the goods were delivered only part way (for example, to Chicago), another entity would not need to substantially re-perform the entity's performance to date—that is, another entity would not need to take the goods back to Vancouver to deliver them to New York City. The boards observed that, in those cases, the assessment of whether another entity would need to substantially re-perform the performance completed to date can be used as an objective basis for determining whether the customer receives benefit from the entity's performance as it is provided.

BC127 The boards decided that an entity should disregard any contractual or practical limitations when it assesses the 'simultaneously receives and consumes' criterion and whether another entity would need to substantially re-perform the performance completed to date. This is because the objective of this criterion is to determine whether control of the goods or services has already been transferred to the customer. This is done by using a hypothetical assessment of what another entity would need to do if it were to take over the remaining performance. Thus, actual practical or contractual limitations on the remaining performance would have no bearing on the assessment of whether the entity has transferred control of the goods or services provided to date.

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BC128 The boards also observed that this criterion is not intended to apply to contracts in which the entity's performance is not immediately consumed by the customer, which would be typical in cases in which the entity's performance results in an asset (such as work-in-progress). Consequently, an entity that applies IFRS 15 to contracts in which the entity's performance results in an asset (which could be intangible) being created or enhanced should consider the criteria in paragraph 35(b) and (c) of IFRS 15.

Performance creates or enhances an asset that the customer controls as it is created (paragraph 35(b))

BC129 The boards included this criterion to address situations in which an entity's performance creates or enhances an asset that a customer clearly controls as the asset is created or enhanced. In those cases, because the customer controls any work in progress, the customer is obtaining the benefits of the goods or services that the entity is providing and, thus, the performance obligation is satisfied over time. For example, in the case of a construction contract in which the entity is building on the customer's land, the customer generally controls any work in progress arising from the entity's performance.

BC130 The boards observed that the basis for this criterion is consistent with the rationale for using the 'percentage-of-completion' revenue recognition approach in previous revenue guidance in US GAAP. That guidance acknowledged that in many construction contracts the entity has, in effect, agreed to sell its rights to the asset (ie work-in-progress) as the entity performs. Accordingly, the parties have agreed, in effect, to a continuous sale (ie the customer controls the work-in-progress) that occurs as the work progresses.

BC131 Many respondents explained that this criterion would be straightforward and helpful in cases in which the customer clearly controls the asset that is being constructed or enhanced. However, the boards observed that for some performance obligations, it may be unclear whether the asset that is created or enhanced is controlled by the customer. Consequently, it may be more challenging to determine when control transfers in those cases and, therefore, the boards developed a third criterion in paragraph 35(c) of IFRS 15.

Performance does not create an asset with an alternative use to the entity and the entity has an enforceable right to payment for performance completed to date (paragraph 35(c))

BC132 The boards observed that, in some cases, applying the criteria in paragraph 35(a) and (b) of IFRS 15 could be challenging. Consequently, the boards developed a third criterion to help with the assessment of control. The boards observed that this criterion may be necessary for services that may be specific to a customer (for example, consulting services that ultimately result in a professional opinion for the customer) but also for the creation of tangible (or intangible) goods.

BC133 The notions of 'alternative use' and 'right to payment' are described in the following paragraphs.

Performance does not create an asset with an alternative use

- BC134 The boards developed the notion of alternative use to exclude the circumstances in which the entity's performance would not result in the transfer of control of goods or services to the customer over time. This is because when the entity's performance creates an asset with an alternative use to the entity, the entity could readily direct the asset to another customer and, therefore, the customer would not control the asset as it is being created. This may occur in the creation of many standard inventory-type items for which the entity has the discretion to substitute across different contracts with customers. In those cases, the customer cannot control the asset because the customer does not have the ability to restrict the entity from directing that asset to another customer.
- BC135 Conversely, when an entity creates an asset that is highly customised for a particular customer, the asset would be less likely to have an alternative use. This is because the entity would incur significant costs to reconfigure the asset for sale to another customer (or would need to sell the asset for a significantly reduced price). In that case, the customer could be regarded as receiving the benefit of that performance and, consequently, as having control of the goods or services (ie the asset being created) as the performance occurs. (However, an entity would also need to consider whether a right to payment exists to conclude that control transfers over time, see paragraphs BC142–BC148.)
- BC136 In assessing whether the asset has an alternative use, the entity would need to consider practical limitations and contractual restrictions on directing the asset for another use. In determining whether the entity is limited practically from directing the asset for another use, the boards decided that an entity should consider the characteristics of the asset that will ultimately be transferred to the customer. This is because, for some assets, it is not the period of time for which the asset has no alternative use that is the critical factor in making the assessment but, instead, whether the asset that is ultimately transferred could be redirected without a significant cost of rework. This may occur in some manufacturing contracts in which the basic design of the asset is the same across all contracts, but the customisation is substantial. Consequently, redirecting the asset in its completed state to another customer would require significant rework.
- BC137 Although the level of customisation might be a helpful factor to consider when assessing whether an asset has an alternative use, the boards decided that it should not be a determinative factor. This is because in some cases (for example, some real estate contracts), an asset may be standardised but may still not have an alternative use to an entity, as a result of substantive contractual restrictions that preclude the entity from readily directing the asset to another customer. If a contract precludes an entity from transferring an asset to another customer and that restriction is substantive, the entity does not have an alternative use for that asset because it is legally obliged to direct the asset to the customer. Consequently, this indicates that the customer controls the asset as it is created, because the customer has the present ability to restrict the entity from directing that asset to another

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customer (an entity would also need to consider whether a right to payment exists to conclude that control of the asset transfers over time as it is created, see paragraphs BC142–BC148). The boards observed that contractual restrictions are often relevant in real estate contracts, but might also be relevant in other types of contracts.

BC138 The boards also noted that contractual restrictions that provide a protective right to the customer would not be sufficient to establish that an asset has no alternative use to the entity. The boards observed that a protective right typically results in the entity having the practical ability to physically substitute or redirect the asset without the customer being aware of or objecting to the change. For example, a contract might state that an entity cannot transfer a good because a customer has legal title to the goods in the contract. However, the customer's legal title to the goods is intended to protect the customer in the event of the entity's liquidation and the entity can physically substitute and redirect the goods to another customer for little cost. In this example, the contractual restriction is merely a protective right and does not indicate that control of the goods have transferred to the customer.

BC139 Some respondents observed that requiring an entity to consider contractual and practical restrictions in paragraph 35(c) of IFRS 15 seems to contradict the requirements in paragraph B4 of IFRS 15 to ignore contractual and practical limitations when applying the criterion in paragraph 35(a) of IFRS 15. The boards noted that this difference is appropriate. Although the objective of both criteria is to assess when control transfers over time, each criterion provides a different method for assessing when that control transfers, because the criteria were designed to apply to different scenarios.

BC140 The boards decided that the assessment of alternative use should be completed only at contract inception and should not be updated. Otherwise, an entity would need to continually reassess whether the asset has an alternative use, which could lead to a pattern of performance (and, therefore, revenue recognition) that is not useful.

BC141 The boards also decided that while the notion of alternative use is a necessary part of the criterion in paragraph 35(c), it is not enough to conclude that a customer controls an asset. Consequently, the boards decided that to demonstrate that a customer controls an asset that has no alternative use as it is being created, an entity must also have an enforceable right to payment for performance completed to date.

The entity has an enforceable right to payment for performance completed to date

BC142 The boards decided that there is a link between the assessment of control and the factors of no alternative use and a 'right to payment'. This is because if an asset that an entity is creating has no alternative use to the entity, the entity is effectively constructing an asset at the direction of the customer. Consequently, the entity will want to be economically protected from the risk of the customer terminating the contract and leaving the entity with no asset or an asset that has little value to the entity. That protection will be established by requiring that if the contract is terminated, the customer must

pay for the entity's performance completed to date. This is consistent with other exchange contracts in which a customer would typically be obliged to pay only if it has received control of goods or services in the exchange. Consequently, the fact that the customer is obliged to pay for the entity's performance (or, in other words, is unable to avoid paying for that performance) suggests that the customer has obtained the benefits from the entity's performance.

- BC143 The boards intended the term 'right to payment' to refer to a payment that compensates an entity for its performance completed to date rather than, for example, a payment of a deposit or a payment to compensate the entity for inconvenience or loss of profit. This is because the underlying objective of the criterion is to determine whether the entity is transferring control of goods or services to the customer as an asset is being created for that customer. Consequently, assuming there is rational behaviour and that there are no broader perceived economic benefits that might exist outside the scope of the contract with the customer, the entity would only agree to transfer control of the goods or services to the customer if the entity is compensated for the costs associated with fulfilling the contract and it receives a profit margin that includes a return on those costs.
- BC144 The boards noted that the compensation to which the entity would be entitled upon termination by the customer might not always be the contract margin, because the value transferred to a customer in a prematurely terminated contract may not be proportional to the value if the contract was completed. However, the boards decided that to demonstrate compensation for performance completed to date, the compensation should be based on a reasonable proportion of the entity's expected profit margin or be a reasonable return on the entity's cost of capital. Furthermore, the boards noted that the focus should be on the amount to which the entity would be entitled upon termination rather than the amount to which the entity might ultimately be willing to settle for in a negotiation. Consequently, the boards clarified their intention about what a 'reasonable profit margin' is intended to represent in paragraph B9 of IFRS 15.
- BC145 In addition, the boards clarified that an entity need not have a present unconditional right to payment but, instead, it must have an enforceable right to demand and/or retain payment for performance completed to date if the customer were to terminate the contract without cause before completion. For example, consider a consulting contract in which the consulting entity agrees to provide a report at the end of the contract for a fixed amount that is conditional on providing that report. If the entity were performing under that contract, it would have a right to payment for performance completed to date if the terms of the contract (or other law) require the customer to compensate the entity for its work completed to date if the customer terminates the contract without cause before completion. The boards clarified this notion because the contractual payment terms in the contract might not always align with the entity's enforceable rights to payment for performance completed to date.

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BC146 A few respondents asked whether a 100 per cent non-refundable upfront payment would meet the 'right to payment for performance completed to date' criterion (ie because a 100 per cent payment would at least compensate the entity for work completed to date throughout the contract). The boards decided that that type of payment would meet that criterion if the entity's right to retain (and not refund) that payment would be enforceable if the customer terminated the contract. Furthermore, the boards noted that the right to payment should be enforceable; otherwise, it is questionable whether the entity actually has a right to payment. Consequently, the boards included the factors in paragraph B12 of IFRS 15 to help an entity determine whether the right to payment would be enforceable.

BC147 The boards also decided to clarify that an entity could have an enforceable right to payment in some cases in which a customer might not have a right to terminate the contract or might have a right to terminate the contract only at specified times. This would be the case if the contract or other laws in the jurisdiction require the entity and the customer to complete their respective obligations (often referred to as specific performance).

Right to payment as a separate revenue recognition criterion

BC148 The boards considered but rejected specifying a right to payment as a more overarching criterion in determining when revenue is recognised, for the following reasons:

- (a) an entity must have a contract to recognise revenue in accordance with IFRS 15 and a component of a contract is a right to payment.
- (b) the core revenue recognition principle is about determining whether goods or services have been transferred to a customer, not whether the entity has a right to payment (although it is an important part of determining whether a contract exists – see paragraphs BC31–BC46). Including a right to payment as an overarching criterion for determining when a performance obligation is satisfied could have potentially overridden that revenue recognition principle.
- (c) a right to payment does not necessarily indicate a transfer of goods or services (for example, in some contracts, customers are required to make non-refundable upfront payments and do not receive any goods or services in exchange). In cases in which the customer clearly receives benefits as the entity performs, as in many service contracts, the possibility that the entity will ultimately not retain the payment for its performance is addressed in the measurement of revenue. For example, in some service contracts in which the customer simultaneously receives and consumes benefits as the entity performs, the customer may be able to terminate the contract and receive a full refund of any consideration paid. The boards decided that in those cases, because the entity is transferring services to the customer, it should recognise revenue subject to an assessment of whether it should constrain the amount of the transaction price to which it is entitled (see paragraphs BC203–BC223).

Agreements for the construction of real estate

- BC149 In developing the requirements for assessing when goods or services transfer to the customer, the boards considered the diversity in practice from applying previous revenue recognition requirements in IFRS that were specific to the construction of real estate. That diversity in practice resulted from the difficulty in determining when control of real estate transferred to the customer over time by applying the previous IFRS revenue recognition criteria to complex contracts with different facts and circumstances.
- BC150 The boards envisage that the diversity in practice should be reduced by the requirements in paragraphs 35–37 of IFRS 15, which provide specific requirements for determining when goods or services transfer over time. However, the boards observe that the pattern of transfer may be different for different real estate contracts because it will depend on the relevant facts and circumstances of each contract. For example, some real estate contracts may result in an asset that cannot (under the terms of the contract) be readily directed to another customer (ie the entity’s performance does not create an asset with an alternative use to the entity), and the contracts require the customer to pay for performance completed to date (thus meeting the criterion in paragraph 35(c) of IFRS 15). However, other real estate contracts that create an asset with no alternative use to the entity may not require the customer to pay for performance completed to date. Therefore, an entity would reach a different conclusion on the pattern of transfer for those contracts.
- BC151 Some respondents applying IFRS in the residential real estate industry supported the addition of the criteria for determining whether a performance obligation is satisfied over time, because they reasoned it would assist them in assessing whether revenue could be recognised over time as construction of residential units in a multi-unit real estate development occurs. Other respondents in this industry explained that although they were able to conclude that their performance does not create an asset with an alternative use, they were unable to meet the ‘right to payment for performance completed to date’ criterion. This would mean that they would be able to recognise revenue only at the point in time when each unit transfers to the customer (often only after construction is complete and the customer has physical possession), which they stated would be an inappropriate depiction of their performance.
- BC152 However, the boards concluded that if either of the criteria in paragraph 35(c) of IFRS 15 is not met, recognising revenue over time would not faithfully depict the entity’s performance and the entity’s and the customer’s respective rights and obligations in the contract. Furthermore, the boards decided that clarifying the ‘no alternative use and right to payment for performance completed to date’ criterion would ensure greater certainty and consistency in recognising revenue for multi-unit residential real estate developments.

**Performance obligations satisfied at a point in time
(paragraph 38)**

- BC153 The boards decided that all performance obligations that do not meet the criteria for being satisfied over time should be accounted for as performance obligations satisfied at a point in time. For performance obligations satisfied at a point in time, the performance obligation is satisfied at the point in time when control of the goods or services transfers to the customer. The boards included indicators of the transfer of control in paragraph 38 of IFRS 15.
- BC154 Many respondents commented that the indicators were useful for contracts for the sales of goods to assist an entity in determining when it has transferred control of an asset (whether tangible or intangible). The boards included the indicator ‘the customer has the significant risks and rewards of ownership of the asset’ because of comments from respondents who disagreed with the boards’ initial proposal to eliminate considerations of the ‘risks and rewards of ownership’ from the recognition of revenue. Respondents observed that risks and rewards can be a helpful factor to consider when determining the transfer of control, as highlighted by the IASB in IFRS 10 *Consolidated Financial Statements*, and can often be a consequence of controlling an asset. The boards decided that adding risks and rewards as an indicator provides additional guidance, but does not change the principle of determining the transfer of goods or services on the basis of the transfer of control.
- BC155 Some respondents questioned whether all of the indicators would need to be present for an entity to conclude that it had transferred control of a good or service. Some respondents also questioned what an entity should do if some but not all of the indicators were present. In their redeliberations, the boards emphasised that the indicators in paragraph 38 of IFRS 15 are not a list of conditions that must be met before an entity can conclude that control of a good or service has transferred to a customer. Instead, the indicators are a list of factors that are often present if a customer has control of an asset and that list is provided to assist entities in applying the principle of control in paragraph 31 of IFRS 15.
- BC156 The boards considered including an indicator that the ‘design or function of the good or service is customer-specific’. However, the boards decided not to include this indicator in IFRS 15, because it would apply mainly to service contracts (for example, construction-type contracts) and it would be unnecessary in the light of the requirements for determining when performance obligations are satisfied over time. As described in paragraphs BC134–BC141, the notion of customer-specific design or function has been developed into the criterion of ‘an asset with no alternative use to the entity’.
- BC157 Respondents also suggested additional indicators such as the entity’s lack of continuing involvement in the good or service (for example, a call option on a delivered good). The boards included application guidance to help an entity assess the transfer of control in circumstances in which put or call options exist in a contract with a customer (see paragraphs BC422–BC433).

Measuring progress towards complete satisfaction of a performance obligation (paragraphs 39–45 and B14–B19)

- BC158 The boards decided that when an entity determines that a performance obligation is satisfied over time, it should determine how much revenue to recognise in each reporting period by measuring its progress towards complete satisfaction of the performance obligation.
- BC159 There are various methods that an entity might use to measure its progress towards complete satisfaction of a performance obligation. Because of the breadth of the scope of IFRS 15, the boards decided that it would not be feasible to consider all possible methods and prescribe when an entity should use each method. Accordingly, an entity should use judgement when selecting an appropriate method of measuring progress towards complete satisfaction of a performance obligation. That does not mean that an entity has a ‘free choice’. The requirements state that an entity should select a method of measuring progress that is consistent with the clearly stated objective of depicting the entity’s performance—that is, the satisfaction of an entity’s performance obligation—in transferring control of goods or services to the customer.
- BC160 To meet that objective of depicting the entity’s performance, an entity would need to consider the nature of the promised goods or services and the nature of the entity’s performance. For example, in a typical health club contract, the entity’s promise is to stand ready for a period of time (ie by making the health club available), rather than providing a service only when the customer requires it. In this case, the customer benefits from the entity’s service of making the health club available. This is evidenced by the fact that the extent to which the customer uses the health club does not, in itself, affect the amount of the remaining goods or services to which the customer is entitled. In addition, the customer is obliged to pay the consideration regardless of whether it uses the health club. Consequently, in those cases, the entity would need to select a measure of progress based on its service of making goods or services available, instead of when the customer uses the goods or services made available to them.
- BC161 The boards decided that an entity should apply the selected method for measuring progress consistently for a particular performance obligation and also across contracts that have performance obligations with similar characteristics. An entity should not use different methods to measure its performance in satisfying the same or similar performance obligations, otherwise that entity’s revenue would not be comparable in different reporting periods. The boards also noted that if an entity were permitted to apply more than one method to measure its performance in fulfilling a performance obligation, it would effectively bypass the requirements for identifying performance obligations.
- BC162 Although the boards did not consider all possible methods and prescribe when an entity should use each method, they observed that there are broadly two methods that the entity might consider when determining the method of measuring progress towards complete satisfaction of the performance

obligation—that is, output and input methods. Requirements for the application of those methods are included in the application guidance (see paragraphs B14–B19 of IFRS 15).

Output methods

- BC163 Output methods recognise revenue on the basis of direct measurements of the value to the customer of the goods or services transferred to date (for example, surveys of performance completed to date, appraisals of results achieved, milestones reached, time elapsed and units delivered or units produced). When applying an output method, ‘value to the customer’ refers to an objective measure of the entity’s performance in the contract. However, value to the customer is not intended to be assessed by reference to the market prices or stand-alone selling prices of the individual goods or services promised in the contract, nor is it intended to refer to the value that the customer perceives to be embodied in the goods or services.
- BC164 The boards decided that, conceptually, an output measure is the most faithful depiction of an entity’s performance because it directly measures the value of the goods or services transferred to the customer. However, the boards observed that it would be appropriate for an entity to use an input method if that method would be less costly and would provide a reasonable proxy for measuring progress.
- BC165 In the redeliberations, some respondents, particularly those in the contract manufacturing industry, requested the boards to provide more guidance on when units-of-delivery or units-of-production methods would be appropriate. Those respondents observed that such methods appear to be output methods and, therefore, questioned whether they would always provide the most appropriate depiction of an entity’s performance. The boards observed that such methods may be appropriate in some cases; however, they may not always result in the best depiction of an entity’s performance if the performance obligation is satisfied over time. This is because a units-of-delivery or a units-of-production method ignores the work in progress that belongs to the customer. When that work in progress is material to either the contract or the financial statements as a whole, the boards observed that using a units-of-delivery or a units-of-production method would distort the entity’s performance because it would not recognise revenue for the assets that are created before delivery or before production is complete but are controlled by the customer.
- BC166 The boards also observed that a units-of-delivery or a units-of-production method may not be appropriate if the contract provides both design and production services because, in this case, each item produced or delivered may not transfer an equal amount of value to the customer. However, a units-of-delivery method may be an appropriate method for measuring progress for a long-term manufacturing contract of standard items that individually transfer an equal amount of value to the customer on delivery. Thus, the boards clarified that in selecting an output method for measuring progress and determining whether a units-of-delivery or a units-of-production method is appropriate, an entity should consider its facts and circumstances and select

the method that depicts the entity's performance and the transfer of control of the goods or services to the customer.

- BC167 The boards also decided that, in some circumstances, as a practical expedient, another appropriate output method is to recognise revenue at the amount of consideration to which an entity has a right to invoice. This method is appropriate if the amount of consideration that the entity has a right to invoice corresponds directly with the value to the customer of each incremental good or service that the entity transfers to the customer (ie the entity's performance completed to date). This may occur, for example, in a services contract in which an entity invoices a fixed amount for each hour of service provided.

Input methods

- BC168 Input methods recognise revenue on the basis of an entity's efforts or inputs towards satisfying a performance obligation (for example, resources consumed, labour hours expended, costs incurred, time elapsed or machine hours used) relative to the total expected inputs to satisfy the performance obligation.
- BC169 In some contracts, an entity promises to transfer both goods and services to a customer, but the customer takes control of the goods, which represent a significant part of the performance obligation, at a different time from that of the services (for example, the customer obtains control of the goods before they are installed). If those goods and services are not distinct, then the entity would have a single performance obligation. Because there is diversity in practice about how to apply an input method to measure progress in such situations, the boards decided to provide additional guidance related to uninstalled materials.

Uninstalled materials

- BC170 The boards decided to clarify that the adjustment to the input method for uninstalled materials is intended to ensure that the input method meets the objective of measuring progress towards complete satisfaction of a performance obligation, as described in paragraph 39 of IFRS 15—that is, to depict an entity's performance.
- BC171 The boards observed that if a customer obtains control of the goods before they are installed by an entity, then it would be inappropriate for the entity to continue to recognise the goods as inventory. Instead, the entity should recognise revenue for the transferred goods in accordance with the core principle of IFRS 15. The boards also observed that if the entity applies a cost-to-cost method of measuring progress (ie costs incurred compared with total expected costs), the entity might (in the absence of clear requirements) include the cost of the goods in the cost-to-cost calculation and, therefore, recognise a contract-wide profit margin for the transfer of the goods. The boards noted that recognising a contract-wide profit margin before the goods are installed could overstate the measure of the entity's performance and, therefore, revenue would be overstated. Alternatively, requiring an entity to estimate a profit margin that is different from the contract-wide profit margin

could be complex and could effectively create a performance obligation for goods that are not distinct (thus bypassing the requirements for identifying performance obligations). Therefore, the boards decided that, in specified circumstances, an entity should recognise revenue for the transfer of the goods but only in an amount equal to the cost of those goods. In those circumstances, an entity should also exclude the costs of the goods from the cost-to-cost calculation to be consistent with the cost-to-cost methodology.

- BC172 The boards noted that the adjustment to the cost-to-cost measure of progress for uninstalled materials is generally intended to apply to a subset of goods in a construction-type contract—that is, only to those goods that have a significant cost relative to the contract and only if the entity is essentially providing a simple procurement service to the customer. For goods that meet the conditions in paragraph B19(b) of IFRS 15, recognising revenue to the extent of the costs of those goods ensures that the depiction of the entity's profit (or margin) in the contract is similar to the profit (or margin) that the entity would recognise if the customer had supplied those goods themselves for the entity to install or use in the construction activity.
- BC173 Some respondents disagreed with the requirements that an entity recognise a profit margin of zero on the transfer of the uninstalled materials to the customer. In their view, recognising different profit margins for different parts of a single performance obligation is inconsistent with the principle of identifying performance obligations. Other respondents disagreed with recognising revenue for uninstalled materials at a zero profit margin because it might not properly depict an entity's rights under the contract (for example, if the entity was entitled on termination of the contract to a payment at an amount that reflects the contract-wide margin for all work performed, including the transfer of uninstalled materials to the customer).
- BC174 The boards considered those arguments but decided that the adjustment to the input method specified in paragraph B19(b) of IFRS 15 will ensure that the input method meets the objective of measuring progress to depict an entity's performance. The boards disagreed with the concern raised by some respondents that paragraph B19(b) of IFRS 15 is inconsistent with the principle of identifying performance obligations. Although the outcome of applying paragraph B19(b) of IFRS 15 is that some goods or services that are part of a single performance obligation attract a margin, while any uninstalled materials attract only a zero margin, that difference arises only as a consequence of the need to adjust the cost-to-cost calculation so that the input method faithfully depicts the entity's performance in the contract.
- BC175 To be consistent with their decision on uninstalled materials, the boards also clarified that if an entity selects an input method such as cost-to-cost to measure its progress, the entity should adjust the measure of progress if including some of those costs incurred (for example, inefficiencies and wasted materials) would distort the entity's performance in the contract.

Inefficiencies and wasted materials

- BC176 Paragraph B19 of IFRS 15 acknowledges that a shortcoming of input methods is that there may not be a direct relationship between an entity's inputs and the transfer of control of goods or services to a customer. This would be the case if the cost-to-cost method includes costs attributable to wasted materials or other inefficiencies that do not contribute to the satisfaction of a performance obligation. Consequently, an entity should exclude the effects of any inputs that do not depict the transfer of control of goods or services to the customer (for example, the costs of wasted materials, labour or other resources to fulfil the contract that were not reflected in the price of the contract). In that regard, the requirements in paragraph B19 of IFRS 15 can be viewed as a reminder that a mechanical application of the cost-to-cost method might not always provide a faithful depiction of the entity's performance.
- BC177 As part of their redeliberations, the boards considered whether more guidance should be provided on the notions of inefficiency and wasted materials. For instance, some respondents asked if the assessment should focus on entity-specific inefficiencies or market-driven inefficiencies, and some requested a clear distinction between the accounting for normal expected wasted materials and the accounting for abnormal wasted materials.
- BC178 The boards acknowledged the concerns but decided that it would not be feasible to develop additional guidance that would clearly and consistently identify the costs of inefficiencies and wasted materials that should be excluded from a cost-to-cost measure of progress. Instead, the boards decided to emphasise that the objective of measuring progress towards complete satisfaction of the performance obligation is to depict an entity's performance in the contract and therefore a cost-to-cost calculation may require adjustment if some of the costs incurred do not contribute to the progress in the contract.

Reasonable measures of progress

- BC179 The boards clarified that when selecting a method to measure progress and, thus, determining when to recognise revenue, an entity should recognise revenue for its performance only if it can reasonably measure its progress towards complete satisfaction of the performance obligation. Some asked whether an entity's inability to measure progress would mean that costs would also be deferred. However, the boards observed that unless the entity can recognise an asset from the costs to fulfil a contract in accordance with paragraph 95 of IFRS 15, those costs would not represent an asset of the entity and, therefore, should be recognised as expenses as they are incurred.
- BC180 The boards also concluded that in cases in which an entity cannot reasonably measure its progress towards complete satisfaction of a performance obligation, but nevertheless expects eventually to recover the costs incurred in satisfying the performance obligation, the entity should recognise at least some amount of revenue to reflect the fact that it is making progress in satisfying the performance obligation. Consequently, the boards decided that in those cases, an entity should recognise revenue for the satisfaction of the performance obligation only to the extent of the costs incurred. (That method

is consistent with previous revenue recognition requirements in both IFRS and US GAAP for measuring progress.) However, the boards also decided that an entity should stop using that method when it can reasonably measure its progress towards complete satisfaction of the performance obligation.

Measurement of revenue (paragraphs 46–90)

BC181 The boards decided that an entity should measure revenue based on an allocated transaction price approach. Using that approach, an entity allocates the transaction price to each performance obligation at an amount that depicts the amount of consideration to which the entity expects to be entitled in exchange for satisfying each performance obligation. That allocation determines the amount of revenue that an entity recognises when (or as) it satisfies each performance obligation. Most respondents supported the allocated transaction price approach.

BC182 The boards considered, but rejected, an alternative measurement approach, which would have been to measure the remaining performance obligations directly at the end of each reporting period. The boards observed that this alternative would have made accounting for the contract more complex. In addition, the boards expected that in many cases it would have provided users of financial statements with little additional information, either because the values of goods or services promised are not inherently volatile or because the effect of any volatility that might exist is limited when an entity transfers the goods or services to the customer over a relatively short time. Paragraphs BC25–BC27 include additional discussion on rejected measurement approaches.

BC183 The allocated transaction price approach generally requires an entity to follow three main steps to determine the amount of revenue that can be recognised for satisfied performance obligations. Those steps are as follows:

- (a) determine the transaction price for the contract;
- (b) allocate the transaction price to performance obligations; and
- (c) recognise revenue at the amount allocated to the satisfied performance obligation.

Determining the transaction price (paragraphs 47–72)

BC184 Determining the transaction price is an important step in the revenue recognition model because the transaction price is the amount that an entity allocates to the performance obligations in a contract and ultimately recognises as revenue.

BC185 The boards decided to define the transaction price as the amount of consideration to which an entity expects to be entitled in exchange for transferring goods or services. Consequently, the objective in determining the transaction price at the end of each reporting period is to predict the total amount of consideration to which the entity will be entitled from the contract. In developing IFRS 15, the boards decided that the transaction price

should not be adjusted for the effects of the customer's credit risk (see paragraphs BC259–BC265) unless the contract includes a significant financing component (see paragraphs BC229–BC247).

- BC186 The boards clarified that the transaction price should include only amounts (including variable amounts) to which the entity has rights under the present contract. For example, the transaction price does not include estimates of consideration from the future exercise of options for additional goods or services or from future change orders. Until the customer exercises the option or agrees to the change order, the entity does not have a right to consideration.
- BC187 The boards also clarified that the amounts to which the entity has rights under the present contract can be paid by any party (ie not only by the customer). For example, in the healthcare industry, an entity may determine the transaction price based on amounts to which it will be entitled to payment from the patient, insurance companies and/or governmental organisations. This may also occur in other industries in which an entity receives a payment from a manufacturer as a result of the manufacturer issuing coupons or rebates directly to the entity's customer. However, it would not include amounts collected on behalf of another party such as some sales taxes and value added taxes in some jurisdictions.
- BC188 Determining the transaction price when a customer promises to pay a fixed amount of cash consideration (ie an amount that will not vary) will be simple. However, determining the transaction price may be more difficult in the following cases:
- (a) the promised amount of consideration is variable (see paragraphs BC189–BC202), which will also require an entity to consider whether it should constrain the estimated amount of consideration to be included in the transaction price (see paragraphs BC203–BC223);
 - (b) the contract has a significant financing component (see paragraphs BC229–BC247);
 - (c) the promised amount of consideration is in a form other than cash (see paragraphs BC248–BC254); and
 - (d) there is consideration payable to the customer by the entity (see paragraphs BC255–BC258).

Clarifications to IFRS 15 (amendments issued in April 2016)—topics for which the IASB decided not to amend IFRS 15 (presentation of sales taxes)

- BC188A Paragraph 47 of IFRS 15 specifies that amounts collected on behalf of third parties, such as some sales taxes, are excluded from the determination of the transaction price. Entities are therefore required to identify and assess sales taxes to determine whether to include or exclude those taxes from the transaction price.

IFRS 15 BC

BC188B After the issuance of Topic 606 and IFRS 15, some US stakeholders expressed concerns about the cost and complexity of assessing tax laws in each jurisdiction, because many entities operate in numerous jurisdictions, and the laws in some jurisdictions are unclear about which party to the transaction is primarily obligated for payment of the taxes. These stakeholders also stated that the variety of, and changes in, tax laws among jurisdictions contributes to that complexity. Consequently, some preparers and auditors asked the boards to amend the Standard to add a practical expedient to reduce the complexity and practical difficulties in assessing whether a sales tax is collected on behalf of a third party. An accounting policy choice to either include or exclude all sales taxes in or from revenue was available in the previous revenue standards under US GAAP.

BC188C The FASB decided to amend Topic 606 to provide an accounting policy election that permits an entity to exclude from the measurement of the transaction price all taxes assessed by a governmental authority that are both imposed on, and concurrent with, a specific revenue-producing transaction and collected from customers (for example, sales taxes, use taxes, value added taxes, and some excise taxes). Taxes assessed on an entity's total gross receipts or imposed during the inventory procurement process are excluded from the scope of the election.

BC188D The IASB decided not to provide a similar accounting policy choice, for the following reasons:

- (a) It would reduce the comparability of revenue between entities operating under different tax regimes in different jurisdictions, as well as between entities operating in the same jurisdictions to the extent that they choose different approaches.
- (b) The previous revenue Standards under IFRS contained requirements applicable to sales tax similar to those in IFRS 15. Consequently, assessing whether sales taxes are collected on behalf of a third party is not a new requirement for IFRS preparers.
- (c) It would create an exception to the revenue recognition model that does not reflect the economics of the arrangement in cases for which a sales (or similar) tax is a tax on the entity rather than a tax collected by the entity from the customer on behalf of a tax authority.

The IASB acknowledged that, because the policy choice is not available in IFRS 15, this gives rise to a difference between IFRS 15 and Topic 606.

Variable consideration (paragraphs 50–59)

BC189 The boards noted that in contracts with customers in which the promised consideration is variable, an entity needs to estimate the amount of consideration to which the entity expects to be entitled. Consequently, the boards decided to provide requirements that address:

- (a) identifying when variable consideration is present in a contract with a customer (see paragraphs BC190–BC194);

- (b) the methods for estimating variable consideration (see paragraphs BC195–BC202);
- (c) when those estimates of variable consideration should be constrained and, thus, not included in the transaction price (see paragraphs BC203–BC223); and
- (d) how to account for subsequent changes in the transaction price (see paragraphs BC224–BC228).

Identifying variable consideration

- BC190 The boards noted that variable consideration can arise in any circumstance in which the consideration to which the entity will be entitled under the contract may vary. The examples in paragraph 51 of IFRS 15 include common types of variable consideration that may occur in a contract with a customer.
- BC191 The boards observed that consideration can be variable even in cases in which the stated price in the contract is fixed. This is because the entity may be entitled to the consideration only upon the occurrence or non-occurrence of a future event. Consider, for example, a fixed-price service contract in which the customer pays upfront and the terms of the contract provide the customer with a full refund of the amount paid if the customer is dissatisfied with the service at any time. In those cases, the consideration is variable because the entity might be entitled to all of the consideration or none of the consideration if the customer exercises its right to a refund.
- BC192 The contract will often specify the terms that result in the consideration being classified as variable. However, in some cases the promised consideration may be variable because the facts and circumstances indicate that the entity may accept a lower price than that stated in the contract (ie the contract contains an implicit price concession). The boards observed that an entity's customary business practices, published policies or specific statements may provide evidence that the entity is willing to accept a lower price in exchange for the promised goods and services. For example, an entity might grant a price concession to a customer for goods that were previously sold to that customer to enable the customer to discount the goods and, therefore, more easily sell them to a third party. The boards noted that in many cases, price concessions are likely to be granted to enhance a customer relationship to encourage future sales to that customer.
- BC193 The boards decided that an entity should also consider all facts and circumstances to determine whether the entity will accept a lower amount of consideration than the price stated in the contract. For example, an entity might enter into a contract with a new customer with a strategy to develop the customer relationship. In that case, although there may not be past evidence that the entity will provide a price concession, there may be other factors present that result in the entity concluding that it will accept a lower price than that stated in the contract.

IFRS 15 BC

BC194 The boards observed that in some cases it may be difficult to determine whether the entity has implicitly offered a price concession or whether the entity has chosen to accept the risk of default by the customer of the contractually agreed-upon consideration (ie customer credit risk). The boards noted that an entity should use judgement and consider all relevant facts and circumstances in making that determination. The boards observed that this judgement was being applied under previous revenue recognition requirements. Consequently, the boards decided not to develop detailed requirements for differentiating between a price concession and impairment losses.

The method for estimating the variable consideration

BC195 The boards decided to specify that an entity should estimate variable consideration using either the expected value or the most likely amount, depending on which method the entity expects will better predict the amount of consideration to which the entity will be entitled (see paragraph 53 of IFRS 15). The boards noted that this is not intended to be a 'free choice'; an entity needs to consider which method it expects to better predict the amount of consideration to which it will be entitled and apply that method consistently for similar types of contracts.

BC196 The boards concluded on the methods to estimate the transaction price in response to the feedback on the 2010 Exposure Draft. That exposure draft proposed that when the consideration in a contract is variable, an entity should measure the transaction price (at its expected value) using only a probability-weighted method. A probability-weighted method reflects the full range of possible consideration amounts, weighted by their respective probabilities. Many respondents to the 2010 Exposure Draft disagreed with measuring the transaction price using a probability-weighted method because they reasoned it would:

- (a) add complexity and be costly to apply; and
- (b) impede the reporting of meaningful results in all circumstances because, for example, it could result in an entity determining the transaction price at an amount of consideration that the entity could never obtain under the contract.

BC197 Some respondents suggested that the boards not specify a measurement model and, instead, require that the transaction price be determined using management's best estimate. Many noted that this would provide management with the flexibility to estimate on the basis of its experience and available information, without the documentation that would be required when a measurement model is specified.

BC198 In their redeliberations, the boards reaffirmed their decision to specify an objective and an appropriate measurement method for estimating the transaction price. This is because specifying an objective and an appropriate measurement method would provide the necessary framework to ensure rigour in the process of estimation. Furthermore, without such a framework,

the measurement of revenue might not be understandable to users of financial statements and might lack comparability between entities.

- BC199 However, in their redeliberations, the boards reconsidered what the appropriate measurement method(s) should be. They noted that a probability-weighted method reflects all of the uncertainties existing in the transaction price at the end of the reporting period. Therefore, it best reflects the conditions that are present at the end of each reporting period. For instance, it reflects the possibility of receiving a greater amount of consideration as well as the risk of receiving a lesser amount. However, the boards observed that users of financial statements are most interested in knowing the total amount of consideration that will ultimately be realised from the contract. Consequently, the boards decided that for the estimate of the transaction price to be meaningful at the end of each reporting period, it should be an amount that the entity expects to better predict the amount of consideration to which it will be entitled (the boards decided to address the issue of credit risk separately – see paragraphs BC259–BC265).
- BC200 The boards observed that in some cases, a probability-weighted estimate (ie an expected value) predicts the amount of consideration to which an entity will be entitled. For example, that is likely to be the case if the entity has a large number of contracts with similar characteristics. However, the boards agreed with respondents that an expected value may not always faithfully predict the consideration to which an entity will be entitled. For example, if the entity is certain to receive one of only two possible consideration amounts in a single contract, the expected value would not be a possible outcome in accordance with the contract and, therefore, might not be relevant in predicting the amount of consideration to which the entity will be entitled. The boards decided that in those cases, another method – the most likely amount method – is necessary to estimate the transaction price. This is because the most likely amount method identifies the individual amount of consideration in the range of possible consideration amounts that is more likely to occur than any other individual outcome.
- BC201 Theoretically, although an entity using the most likely amount method must consider all possible outcomes to identify the most likely one, in practice, there is no need to quantify the less probable outcomes. Similarly, in practice, estimating the expected value using a probability-weighted method does not require an entity to consider all possible outcomes using complex models and techniques, even if an entity has extensive data and can identify many outcomes. In many cases, a limited number of discrete outcomes and probabilities can often provide a reasonable estimate of the distribution of possible outcomes. Therefore, the boards decided that neither of the two approaches should be too costly or complex to apply.
- BC202 The boards also decided that, to provide better information to users, an entity should apply one method consistently throughout the contract when estimating the effect of an uncertainty on the amount of variable consideration to which the entity expects to be entitled. However, the boards observed that this would not mean an entity would need to use one method to

measure each uncertainty in a single contract. Instead, an entity may use different methods for different uncertainties.

Constraining estimates of variable consideration

BC203 The boards decided that to provide useful information to users of financial statements, some estimates of variable consideration should not be included in the transaction price. This would be the case if the estimate of variable consideration (and consequently the amount of revenue recognised) is too uncertain and, therefore, may not faithfully depict the consideration to which the entity will be entitled in exchange for the goods or services transferred to the customer. In that case, the boards decided that an entity should constrain the estimate of variable consideration to be included in the transaction price.

BC204 Many respondents agreed that it was necessary to include some form of constraint on the recognition of revenue that results from variable consideration because a significant portion of errors in financial statements under previous revenue recognition requirements have related to the overstatement or premature recognition of revenue. However, the boards noted that their intention was not to eliminate the use of estimates, which are commonplace and necessary in financial reporting, but instead to ensure that those estimates are robust and result in useful information. This is because revenue is an important metric and users of financial statements explained that it is critical that those estimates of variable consideration be included in revenue only when there is a high degree of confidence that revenue will not be reversed in a subsequent reporting period.

BC205 In developing the requirements for constraining estimates of variable consideration, the boards considered the following:

- (a) the objective of constraining estimates of variable consideration and specifying a level of confidence (see paragraphs BC206–BC213);
- (b) application of the requirements for constraining estimates of variable consideration and sales-based and usage-based royalties on licences of intellectual property (see paragraphs BC214–BC219); and
- (c) whether the requirements for constraining estimates of variable consideration should be included in the determination of the transaction price (Step 3 of the revenue recognition model) or the determination of the cumulative amount of revenue recognised when a performance obligation is satisfied (Step 5 of the revenue recognition model) (see paragraphs BC220–BC223).

The objective of constraining estimates of variable consideration and specifying a level of confidence

BC206 In their redeliberations, the boards decided that it would be helpful to clarify the objective for constraining estimates of variable consideration. In making their decision, the boards considered the feedback received from users of financial statements. The majority of users of financial statements that were consulted 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. This is because an amount that would not reverse in the future would help users of financial statements better predict future revenues of an entity. Therefore, the boards decided that the focus for constraining revenue should be on possible downward adjustments (ie revenue reversals), rather than on all revenue adjustments (ie both downward and upward adjustments). Specifically, the boards decided that an entity should include some or all of an estimate of variable consideration in the transaction price only to the extent it is highly probable that a significant revenue reversal will not occur.

- BC207 The boards acknowledge that the requirement to constrain estimates of variable consideration and the objective they have defined creates a tension with the notion of neutrality in the boards' respective conceptual frameworks. This is because the boards' decision introduces a downward bias into estimates that will be included in the transaction price. However, the boards decided that this bias was reasonable because users of financial statements indicated that revenue is more relevant if it is not expected to be subject to significant future reversals.
- BC208 In the redeliberations, preparers and auditors indicated that meeting the objective of constraining estimates of variable consideration would be difficult if no level of confidence was specified, for instance, if the boards merely specified that an entity should include variable consideration to the extent that it expects that doing so would not result in a significant revenue reversal. Many also observed that omitting a level of confidence from the objective could result in diversity in practice if entities interpreted the implicit confidence level in different ways (for example, some might interpret the implicit confidence level as virtually certain while others might presume it to mean more likely than not).
- BC209 Consequently, the boards decided that specifying a level of confidence would provide clarity and thus ensure more consistent application of the requirements to constrain estimates of variable consideration. In determining the appropriate level of confidence, the boards considered whether they could use the proposal in the 2011 Exposure Draft that constrained revenue to the amount to which an entity would be reasonably assured to be entitled. However, many respondents to the 2011 Exposure Draft were unsure about what the boards intended by using the term 'reasonably assured'. Those respondents observed that the term is used elsewhere in IFRS, US GAAP and auditing requirements and further noted that its meaning is often interpreted differently in those contexts.
- BC210 The boards also considered using terminology that has not previously been used in IFRS and US GAAP. However, the boards decided that any new term that was used might result in diversity in practice, because entities might interpret the new term in different ways. Consequently, the boards decided that the most appropriate level of confidence would be 'highly probable' for IFRS and 'probable' for US GAAP as a result of the usage of those terms in existing requirements.

IFRS 15 BC

- BC211 The boards observed that the term ‘probable’ is widely used and understood in practice in the United States and is defined in US GAAP as ‘the future event or events are likely to occur’ (Topic 450). In contrast, the term ‘probable’ is defined in IFRS as ‘more likely than not’ (IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*). Therefore, to achieve the same meaning in IFRS as US GAAP, the boards decided to use the term ‘highly probable’ for IFRS purposes and ‘probable’ for US GAAP purposes. The boards noted that this is consistent with the approach that the IASB adopted in developing IFRS 5, for which the IASB used the term ‘highly probable’ to achieve the same meaning as ‘probable’ in US GAAP (see paragraph BC81 of IFRS 5).
- BC212 The boards observed that the analysis an entity would undertake to determine if its estimate met the required level of confidence would still be largely qualitative. Specifically, that analysis would require the entity to use judgement and consider the factors in paragraph 57 of IFRS 15 to assess whether it was highly probable that a significant revenue reversal would not occur. In other words, the boards did not expect that an entity would need to prepare a quantitative analysis each time it assessed the likelihood of whether a significant revenue reversal could occur. Therefore, the boards concluded that including a confidence level would not result in application of the requirements that is too costly or complex.
- BC213 The factors in paragraph 57 of IFRS 15 were derived in part from previous requirements in US GAAP on estimating sales returns. Those indicators were also proposed in the 2010 and the 2011 Exposure Drafts and respondents generally agreed that the indicators were relevant and helpful. In their redeliberations, the boards also decided to add an indicator in paragraph 57(d) of IFRS 15 to address the circumstances in which there is no explicit requirement to adjust the price stated in the contract, but the entity has a past practice of offering a broad range of price concessions (or similar types of price adjustments). This is because the boards observed that a practice of offering a broad range of price concessions would increase the probability that a significant revenue reversal would occur if the entity included the contractual amount of consideration in the transaction price.

Application of the requirements to constrain estimates of variable consideration

- BC214 The requirements for constraining estimates of variable consideration first require an entity to estimate the consideration to which the entity will be entitled (see paragraph 53 of IFRS 15). The entity then assesses whether the objective of the requirements for constraining estimates of variable consideration can be met—that is by determining whether it is highly probable that a significant revenue reversal will not occur when the uncertainty associated with the variable consideration is subsequently resolved. If the entity determines that it is highly probable that the inclusion of its estimate will not result in a significant revenue reversal, that amount is included in the transaction price.

- BC215 Although some respondents explained that they reasoned that these requirements would inappropriately require a two-step process, the boards observed that an entity would not be required to strictly follow those two steps if the entity's process for estimating variable consideration already incorporates the principles on which the requirements for constraining estimates of variable consideration are based. For example, an entity might estimate revenue from sales of goods with a right of return. In that case, the entity might not practically need to estimate the expected revenue and then apply the constraint requirements to that estimate, if the entity's calculation of the estimated revenue incorporates the entity's expectations of returns at a level at which it is highly probable that the cumulative amount of revenue recognised would not result in a significant revenue reversal.
- BC216 The requirements for constraining estimates of variable consideration require an entity to assess whether a significant revenue reversal would not occur for the amount of cumulative revenue recognised for a satisfied (or partially satisfied) performance obligation. This is because the boards did not intend for an entity to inappropriately recognise revenue by offsetting the risk of a future revenue reversal for a satisfied (or partially satisfied) performance obligation against expected revenue from future performance.
- BC217 The requirements for constraining estimates of variable consideration also require an entity to assess the magnitude of a significant revenue reversal for both variable consideration and fixed consideration. For example, if the consideration for a single performance obligation included a fixed amount and a variable amount, the entity would assess the magnitude of a possible revenue reversal of the variable amount relative to the total consideration (ie variable and fixed consideration). This is because the objective of constraining estimates of variable consideration is focused on a possible revenue reversal of the amount of cumulative revenue recognised for a performance obligation, rather than on a reversal of only the variable consideration allocated to that performance obligation.
- BC218 The boards noted that in some cases, when an entity applies the requirements for constraining estimates of variable consideration, the entity might determine that it should not include the entire estimate of the variable consideration in the transaction price when it is not highly probable that doing so would not result in a significant revenue reversal. However, the entity might determine that it is highly probable that including some of the estimate of the variable consideration in the transaction price would not result in a significant revenue reversal. The boards decided that, in such cases, the entity should include that amount in the estimate of the transaction price. Respondents to both the 2010 and the 2011 Exposure Drafts supported including some of the variable consideration in the transaction price (and therefore recognising that portion as revenue when the entity satisfies the related performance obligation) if including that amount would meet the objective of the requirements for constraining estimates of variable consideration.

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BC219 However, the boards decided that for a licence of intellectual property for which the consideration is based on the customer's subsequent sales or usage, an entity should not recognise any revenue for the uncertain amounts until the uncertainty is resolved (ie when the customer's subsequent sales or usage occurs). The boards included these requirements because both users and preparers of financial statements generally indicated that if an entity recognised a minimum amount of revenue for those contracts it would not provide relevant information (see paragraphs BC419–BC421).

Constraining the estimate of the transaction price (Step 3) or constraining the cumulative amount of revenue that is recognised (Step 5)

BC220 During the development of the requirements for constraining estimates of variable consideration, the boards considered where in the revenue recognition model it would be most appropriate to apply those requirements.

BC221 Some respondents suggested that if the objective is to constrain the measurement of revenue, it might be more appropriate to constrain the transaction price (ie include a constraint at Step 3). In contrast, if the objective is to limit the amount of revenue recognised, it might be more appropriate to constrain the cumulative amount of revenue recognised (ie include a constraint at Step 5). However, the boards observed that those are not truly independent objectives because the measurement of revenue determines the amount of revenue recognised. In other words, the requirements for constraining estimates of variable consideration restrict revenue recognition and use measurement uncertainty as the basis for determining if (or how much) revenue should be recognised. The boards noted that applying the requirements for constraining estimates of variable consideration to the transaction price or to the cumulative amount of revenue recognised should have an equal effect on the amount of revenue recognised in a contract.

BC222 Consequently, the boards decided that the requirements for constraining estimates of variable consideration should be incorporated into the determination of the transaction price because feedback from respondents indicated that this would be consistent with the way in which management often considers variable consideration.

BC223 Respondents in the asset management and hotel management industries questioned whether constraining the transaction price would result in a pattern of revenue recognition that would faithfully depict their performance under the contract. In many of the contracts in those industries, when a portion of the variable consideration becomes fixed, it relates only to the performance for the period. The boards observed that the requirements for allocating variable consideration (see paragraphs BC284–BC293) would ensure that the revenue recognised would faithfully depict the performance in such a contract.

Subsequent changes in the transaction price

- BC224 After contract inception, an entity will revise its expectations about the amount of consideration to which it expects to be entitled as uncertainties are resolved or as new information about remaining uncertainties becomes available. To depict conditions that exist at the end of each reporting period (and changes in conditions during the reporting period), the boards decided that an entity should update its estimate of the transaction price throughout the contract. The boards concluded that reflecting current assessments of the amount of consideration to which the entity expects to be entitled will provide more useful information to users of financial statements than retaining the initial estimates, especially for long-term contracts that are subject to significant changes in conditions during the life of the contract.
- BC225 The boards considered whether an entity should do either of the following if the transaction price changes during a contract:
- (a) recognise those changes in profit or loss when the changes occur; or
 - (b) allocate those changes to performance obligations.
- BC226 The boards rejected the alternative of recognising the entire amount of a change in the estimate of the transaction price in profit or loss when that change occurs. In the boards' view, that alternative could have resulted in a pattern of revenue recognition that would not faithfully depict the pattern of the transfer of goods or services. Moreover, recognising revenue immediately (and entirely) for a change in the estimate of the transaction price would have been prone to abuse in practice. The boards considered whether changes in the estimate of the transaction price could be presented as a gain or loss separately from revenue, thus preserving the pattern of revenue recognition. However, the boards rejected that alternative because the total amount of revenue recognised for the contract would not have equalled the amount of consideration to which the entity was entitled under the contract.
- BC227 Instead, the boards decided that an entity should allocate a change in the transaction price to all the performance obligations in the contract, subject to the conditions in paragraphs 87–90 of IFRS 15 (see paragraph BC286). This is because the cumulative revenue recognised will then depict the revenue that the entity would have recognised at the end of the subsequent reporting period, if the entity had the information at contract inception. Consequently, the transaction price that is allocated to performance obligations that have already been satisfied should be recognised as revenue (or as a reduction of revenue) immediately.
- BC228 The boards noted that in some cases, an entity might make an estimate of the amount of variable consideration to include in the transaction price at the end of a reporting period. However, information relating to the variable consideration might arise between the end of the reporting period and the date when the financial statements are authorised for issue. The boards decided not to provide guidance on the accounting in these situations because they noted that the accounting for subsequent events is already addressed in IAS 10 *Events after the Reporting Period* and Topic 855 *Subsequent Events*.

The existence of a significant financing component in the contract (paragraphs 60–65)

BC229 Some contracts with customers include a financing component. The financing component may be explicitly identified in the contract or may be implied by the contractual payment terms of the contract. A contract that has a financing component includes, conceptually, two transactions – one for the sale and one for the financing. The boards decided to require an entity to adjust the promised amount of consideration for the effects of financing components if those financing components are significant, for the following reasons:

- (a) not recognising a financing component could misrepresent the revenue of a contract. For example, if a customer pays in arrears, ignoring the financing component of the contract would result in full revenue recognition on the transfer of the good or service, despite the fact that the entity is providing a service of financing to the customer.
- (b) in some contracts, entities (or customers) consider the timing of the cash flows in a contract. Consequently, identifying a significant financing component acknowledges an important economic feature of the contract, which is that the contract includes a financing arrangement as well as the transfer of goods or services. A contract in which the customer pays for a good or service when that good or service is transferred to the customer may be significantly different from a contract in which the customer pays before or after the good or service is transferred in order to provide or receive a financing benefit.

BC230 The objective of adjusting the promised amount of consideration for the effects of a significant financing component is to reflect, in the amount of revenue recognised, the 'cash selling price' of the underlying good or service at the time that the good or service is transferred. The boards observed that adjusting the promised consideration to obtain the cash selling price may only be required when the timing of payments specified in the contract provides the customer or the entity with a significant benefit of financing the transfer of goods or services to the customer. This is because, in other cases, the timing of payments may be for a purpose other than financing, such as protection for non-performance. This is described further in the following paragraphs.

Determining whether a contract includes a significant financing component

BC231 The boards considered whether the requirements for identifying a financing component should be based only on whether payment is due either significantly before, or significantly after, the transfer of goods or services to the customer. However, a number of respondents explained that this might have required an entity to adjust for the time value of money when the parties did not contemplate a financing arrangement as part of the negotiated terms of the contract. Those respondents explained that, in some cases, although there is a significant period of time between the transfer of the goods or services and the payment, the reason for that timing difference is not related to a financing arrangement between the entity and the customer. The boards agreed with those respondents and clarified their intention by specifying in

paragraph 60 of IFRS 15 that an entity should adjust for financing only if the timing of payments specified in the contract provides the customer or the entity with a significant benefit of financing.

BC232 The boards also decided to remove the term ‘time value of money’ from the discussion about adjustments for financing components, to reflect their decision that the focus is on whether the payment terms provide the customer or the entity with a significant benefit of financing. This is because the term ‘time value of money’ is a broader economic term that may suggest that it is necessary to adjust the promised amount of consideration in circumstances other than when the cash sales price may differ from the contractual payments. In addition, the boards decided to refine the factors in paragraph 61 of IFRS 15 that an entity should consider when deciding whether a contract includes a significant financing component. Those factors require evaluation of:

- (a) the difference, if any, between the amount of promised consideration and the cash selling price of the promised goods or services. If the entity (or another entity) sells the same good or service for a different amount of consideration depending on the timing of the payment terms, this generally provides observable data that the parties are aware that there is a financing component in the contract. This factor is presented as an indicator because in some cases the difference between the cash selling price and the consideration promised by the customer is due to factors other than financing (see paragraph BC233).
- (b) the combined effect of (1) the expected length of time between when the entity transfers the promised goods or services to the customer and when the customer pays for those goods or services and (2) the prevailing interest rates in the relevant market. Although the boards decided that the difference in timing between the transfer of goods and services and payment for those goods and services is not determinative, the combined effect of timing and the prevailing interest rates may provide a strong indication that a significant benefit of financing is being provided.

BC233 In addition, the boards included criteria in paragraph 62 of IFRS 15 to clarify the circumstances in which a contract does *not* provide the customer or the entity with a significant benefit of financing:

- (a) the customer has paid for the goods or services in advance and, the timing of the transfer of those goods or services is at the discretion of the customer. The boards noted that for some types of goods or services, such as prepaid phone cards and customer loyalty points, the customer will pay for those goods or services in advance and the transfer of those goods or services to the customer is at the customer’s discretion. The boards expected that, in those cases, the purpose of the payment terms is not related to a financing arrangement between the parties. In addition, the boards decided that the costs of requiring an entity to account for the time value of money in these cases would outweigh any perceived benefit because the entity would need to

continually estimate when the goods or services will transfer to the customer.

- (b) a substantial amount of the consideration promised by the customer is variable and that consideration varies on the basis of factors that are outside the control of the customer or the entity. The boards observed that for some arrangements, the primary purpose of the specified timing or amount of the payment terms might not be to provide the customer or the entity with a significant benefit of financing but, instead, to resolve uncertainties that relate to the consideration for the goods or services. For example, in a royalty arrangement, the entity and the customer might not be willing to fix the price and timing of payment because there are significant uncertainties about the goods or services. The primary purpose of those payment terms may be to provide the parties with assurance of the value of the goods or services rather than to provide significant financing to the customer.
- (c) the difference between the promised consideration and the cash selling price of the good or service arises for reasons other than the provision of financing to either the customer or the entity. In some circumstances, a payment in advance or in arrears in accordance with the typical payment terms of an industry or jurisdiction may have a primary purpose other than financing. For example, a customer may retain or withhold some consideration that is payable only on successful completion of the contract or on achievement of a specified milestone. Alternatively, the customer might be required to pay some consideration upfront to secure a future supply of limited goods or services. The primary purpose of those payment terms may be to provide the customer with assurance that the entity will complete its obligations satisfactorily under the contract, rather than to provide financing to the customer or the entity respectively.

BC234 The boards also observed that for many contracts, an entity will not need to adjust the promised amount of customer consideration because the effects of the financing component will not materially change the amount of revenue that should be recognised in relation to a contract with a customer. In other words, for those contracts, the financing component will not be significant. During their redeliberations, the boards clarified that an entity should consider only the *significance* of a financing component at a contract level rather than consider whether the financing is *material* at a portfolio level. The boards decided that it would have been unduly burdensome to require an entity to account for a financing component if the effects of the financing component were not material to the individual contract, but the combined effects for a portfolio of similar contracts were material to the entity as a whole.

Practical reliefs from the significant financing component requirements

- BC235 Some previous requirements required an entity to recognise the effects of a significant financing component with a customer only if the time period exceeded a specified period, often one year. For example, Subtopic 835-30 *Interest—Imputation of Interest*, excluded ‘transactions with customers or suppliers in the normal course of business that are due in customary trade terms not exceeding approximately one year’. The boards decided to include similar relief in IFRS 15 from the requirements to account for a significant financing component in circumstances in which the period between when the entity transfers the promised goods or services to the customer, and when the customer pays for those goods or services, is one year or less (see paragraph 63 of IFRS 15). The boards observed that, as with the other practical expedients in IFRS 15, an entity should apply the practical expedient consistently to similar contracts in similar circumstances.
- BC236 The boards acknowledged that the relief could produce arbitrary outcomes in some cases because the financing component could be material for short-term contracts with high implicit interest rates and, conversely, could be immaterial for long-term contracts with low implicit interest rates. However, the boards decided to exempt an entity from accounting for the effects of any significant financing component on contracts with an expected duration of one year or less for the following reasons:
- (a) application of IFRS 15 would be simplified. This is because an entity would not be required to:
 - (i) conclude whether those contracts contain the attributes of a financing component that are significant to those contracts (see paragraph BC232); and
 - (ii) determine the interest rate that is implicit within those contracts.
 - (b) the effect on the pattern of profit recognition should be limited because the exemption would apply only to financing arrangements that are expected to expire within 12 months (ie when either the customer pays or the entity performs).
- BC237 Some respondents also suggested that the boards should exempt an entity from reflecting in the measurement of the transaction price the effect of a significant financing component associated with advance payments from customers. Those respondents commented that accounting for any effects of a significant financing component arising from advance payments would result in the following:
- (a) change previous practices in which entities typically did not recognise the effects of the financing implicit in advance payments;

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- (b) revenue that is higher than the cash received (for example, if the discount rate implicit in the contract resulted in the accretion of interest of CU21⁵ over two years, revenue would be recognised in the amount of the CU121 rather than the CU100 in cash that was paid in advance); and
- (c) not reflect the economics of the arrangement when the customer pays in advance for reasons other than financing (for example, the customer has significant credit risk or is compensating the entity for incurring upfront contract costs).

BC238 The boards decided not to exempt an entity from accounting for the effects of a significant financing component for advance payments. This is because ignoring the effects of advance payments could substantially skew the amount and pattern of profit recognition if the advance payment is significant and the primary purpose of that payment is to provide financing to the entity. Consider the example in which an entity requires a customer to pay in advance for a long-term construction contract, because the entity requires financing to obtain materials for the contract. If the entity did not require the customer to pay in advance, the entity would need to obtain the financing from a third party and, consequently, would charge the customer a relatively higher amount to cover the finance costs incurred. However, in either scenario the goods or services transferred to the customer are the same; it is only the party providing the financing to the entity that changes. Consequently, the entity's revenue should be consistent regardless of whether it receives the significant financing benefit from the customer or from a third party.

Discount rate

BC239 The boards considered whether the discount rate used to adjust the promised amount of consideration for the effects of a significant financing component should be a risk-free rate or a risk-adjusted rate. A risk-free rate would have been observable and simple to apply in many jurisdictions and it would have avoided the costs of determining a rate specific to each contract. However, the boards decided that using a risk-free rate would not result in useful information, because the resulting interest rate would not have reflected the characteristics of the parties to the contract. In addition, the boards noted that it would not necessarily have been appropriate to use any rate explicitly specified in the contract because the entity might offer 'cheap' financing as a marketing incentive and, therefore, using that rate would not have resulted in an appropriate recognition of profit over the life of the contract. Consequently, the boards decided that an entity should apply the rate used in a financing transaction between the entity and its customer that does not involve the provision of goods or services because that rate reflects the characteristics of the party receiving financing in the contract. That rate also reflects the customer's creditworthiness, among other risks.

⁵ Monetary items in the Basis for Conclusions are denominated as 'currency units' (CU).

- BC240 Some respondents mentioned that determining the discount rate that would be used in a separate financing transaction between an entity and a customer would be difficult and costly because most entities within the scope of IFRS 15 do not enter into separate financing transactions with their customers. In addition, it would have been impractical for entities with large volumes of customer contracts to determine a discount rate specifically for each individual customer.
- BC241 The boards addressed many of those concerns by providing both the exemption for contracts with a term of up to one year from being considered to have a significant financing component and the factors in paragraph 62 of IFRS 15, which describe when there is no significant financing component that needs to be accounted for. The boards expect that in those remaining contracts in which an entity is required to account separately for the financing component, the entity and its customer will typically negotiate the contractual payment terms separately after considering factors such as inflation rates and the customer's credit risk. Therefore, an entity should have access to sufficient information to determine the discount rate that would be used in a separate financing between the entity and the customer.

Re-evaluating the discount rate used for a significant financing component

- BC242 Some respondents asked whether an entity would be required to revise the discount rate used in determining the amount of a significant financing component if there was a change in circumstances.
- BC243 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.

Presentation of the effect of a significant financing component

- BC244 As a result of the boards' decision on the existence of a significant financing component (see paragraphs BC229–BC243), a contract with a customer that has a significant financing component would be separated into a revenue component (for the notional cash sales price) and a loan component (for the effect of the deferred or advance payment terms). Consequently, the accounting for a trade receivable arising from a contract that has a significant financing component should be comparable to the accounting for a loan with the same features. Consider the following example: Customer A purchases a good on credit and promises to pay CU1,000 in three years. The present value of this trade receivable is CU751. Now consider Customer B who borrows CU751 from a bank with a promise to pay CU1,000 in three years. Customer B uses the loan to purchase the same good as Customer A. Economically, those transactions are the same, but, in the absence of the requirements in IFRS 15 to account for a significant financing component, the form of the transaction would determine whether an entity would recognise revenue of CU751 or

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CU1,000 (ie on a discounted or an undiscounted basis). For this reason, paragraphs 60–65 of IFRS 15 require a contract with a financing component that is significant to the contract to be separated, which results in the same revenue recognition for both transactions.

BC245 The boards observed that the presentation, in the statement of comprehensive income, of any impairment losses from long-term trade receivables (ie receivables arising from the financing components of contracts with customers) would be consistent with the presentation of impairment losses for other types of financial assets within the scope of the boards' respective financial instruments Standards. The boards decided that impairment losses on short-term trade receivables (ie receivables arising from contracts with customers that do not have separately identified financing components) should be presented in the statement of comprehensive income in a consistent manner with impairment losses on long-term trade receivables (see paragraphs BC259–BC265).

BC246 The boards decided that an entity should present the effect of the financing (ie the unwinding of the discount) separately from revenue from contracts with customers, as interest revenue or interest expense, rather than as a change to the measurement of revenue. This is because contracts with financing components that are significant have distinct economic characteristics—one relating to the transfer of goods or services to the customer and one relating to a financing arrangement—and those characteristics should be accounted for and presented separately.

BC247 The boards noted that some entities (for example, banks and other entities with similar types of operations) regularly enter into financing transactions and, therefore, interest represents income arising from ordinary activities for those entities. The boards noted that the requirements in paragraph 65 of IFRS 15 do not preclude an entity from presenting interest as a type of revenue in circumstances in which the interest represents income from the entity's ordinary activities.

Non-cash consideration (paragraphs 66–69)

BC248 When an entity receives cash from a customer in exchange for a good or service, the transaction price and, therefore, the amount of revenue, should be the amount of cash received (ie the value of the inbound asset). To be consistent with that approach, the boards decided that an entity should measure non-cash consideration at fair value. The non-cash consideration could be in the form of goods or services, but it may also be in the form of a financial instrument or property, plant and equipment. For example, an entity might receive an electrical substation in exchange for connecting houses in a new residential development to the electricity network.

BC249 The boards decided that if an entity cannot reasonably estimate the fair value of the non-cash consideration, it should measure the promised consideration indirectly by reference to the stand-alone selling price of the goods or services promised in exchange for the consideration. That approach is consistent both with requirements in previous revenue Standards in IFRS and with

requirements for other situations in which the fair value of the assets surrendered in exchange for assets received may be estimated more reliably. (For instance, IFRS 2 *Share-based Payment* and Subtopic 505-50 *Equity-Based Payments to Non-Employees* state that if the fair value of the goods or services received cannot be estimated reliably, then the entity measures them indirectly by reference to the fair value of the granted equity instrument.)

- BC250 Some respondents observed that estimates of fair value of non-cash consideration may vary like other types of variable consideration that the entity will receive in cash. For example, an entity's entitlement to a bonus that will be received in non-cash consideration may also depend on the occurrence or non-occurrence of a future event. Consequently, those respondents asked the boards to clarify whether the requirements for constraining estimates of variable consideration (see paragraphs 56–58 of IFRS 15) should be applied to estimates of the fair value of non-cash consideration.
- BC251 The boards observed that while the fair value of the non-cash consideration could change because of the occurrence or non-occurrence of a future event, it could also vary because of the form of the consideration. That is, the fair value could vary because of changes in the price or value of the non-cash consideration, such as a change in the price per share.
- BC252 The boards decided that it would be most appropriate to apply the requirements for constraining estimates of variable consideration to the same types of variability regardless of whether the amount that will be received will be in the form of cash or non-cash consideration. Consequently, the boards decided to constrain variability in the estimate of the fair value of the non-cash consideration if that variability relates to changes in the fair value for reasons other than the form of the consideration (ie for reasons other than changes in the price of the non-cash consideration). For example, if an entity is entitled to a performance bonus that is payable in the form of non-cash consideration, the entity would apply the requirements for constraining estimates of variable consideration to the uncertainty of whether the entity will receive the bonus, because that uncertainty is related to something other than the form of the consideration (ie the entity's performance). The boards observed that this principle is not that different from previous revenue recognition requirements under US GAAP for changes in the fair value of equity instruments that are granted as consideration in exchange for goods or services, although those requirements differentiated between the variability on the basis of performance conditions and market conditions (which were defined terms in those requirements).
- BC253 The boards also observed that once recognised, any asset arising from the non-cash consideration would be measured and accounted for in accordance with other relevant requirements (for example, IFRS 9 or Topic 320 *Investments – Debt and Equity Securities* or Topic 323 *Equity Method And Joint Ventures*).

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BC254 The FASB noted that the requirements in Topic 606 will result in the removal of previous requirements for the accounting for share-based payments received by an entity in exchange for goods or services. Those previous requirements provided detailed guidance for the measurement and recognition of revenue when the consideration was in the form of shares or share options. However, the FASB decided to remove those requirements because equity instruments are merely another form of non-cash consideration. Therefore, equity instruments received as promised consideration in a contract with a customer would be accounted for consistently with other forms of non-cash consideration.

Clarifications to IFRS 15 (amendments issued in April 2016)—topics for which the IASB decided not to amend IFRS 15

BC254A The TRG discussed the following implementation questions raised by stakeholders in connection with applying IFRS 15 to contracts that involve non-cash consideration:

- (a) At which date should the fair value of non-cash consideration be measured in determining the transaction price?
- (b) How should the constraint on variable consideration be applied to transactions for which the fair value of non-cash consideration might vary due to both the form of the consideration and for other reasons?

Date of measurement of non-cash consideration

BC254B Paragraph 66 of IFRS 15 requires non-cash consideration to be measured at fair value (or by reference to the stand-alone selling price of the goods or services promised to the customer if an entity cannot reasonably estimate fair value of the non-cash consideration). The TRG's discussion informed the boards that the measurement date for non-cash consideration is unclear and could be interpreted as one of several dates: (a) at contract inception; (b) when the non-cash consideration is received; or (c) at the earlier of when the non-cash consideration is received and when the related performance obligation is satisfied.

BC254C In its discussions, the IASB observed that this issue has important interactions with other Standards (including IFRS 2 *Share-based Payment* and IAS 21 *The Effects of Changes in Foreign Exchange Rates*) and, thus, any decisions made would create a risk of potential unintended consequences. Accordingly, the IASB decided that, if needed, issues relating to the measurement of non-cash consideration should be considered more comprehensively in a separate project.

BC254D The FASB decided to amend the guidance in Topic 606 to require non-cash consideration to be measured at its fair value at contract inception. In the FASB's view, measuring non-cash consideration at contract inception is most consistent with the requirements in Topic 606 on determining the transaction price and on allocating the transaction price to performance obligations. The FASB also expects this approach to be typically less costly and less complex to apply in practice than other alternatives.

BC254E The IASB acknowledged that, because it has concluded that a change equivalent to that decided by the FASB is not needed, the use of a measurement date other than contract inception would not be precluded under IFRS. Consequently, it is possible that diversity between IFRS and US GAAP entities could arise in practice. The IASB observed that, unlike US GAAP, existing IFRS does not contain any specific requirements about the measurement date for non-cash consideration for revenue transactions. In addition, discussions with some stakeholders highlighted that any practical effect of different measurement dates would arise in only limited circumstances. The IASB also noted that paragraph 126 of IFRS 15 requires an entity to disclose information about the methods, inputs and assumptions used for measuring non-cash consideration.

Application of the variable consideration constraint to changes in fair value of non-cash consideration

BC254F The TRG discussed the concerns raised by some stakeholders that it is not clear whether the variable consideration requirements in paragraphs 56–58 of IFRS 15 apply in circumstances in which the fair value of non-cash consideration varies due to both the form of the consideration and for other reasons. In particular, some stakeholders are concerned that bifurcating the effects of variability might be challenging in some circumstances.

BC254G The FASB decided to amend Topic 606 to specify that the constraint on variable consideration applies only to variability that arises for reasons other than the form of the consideration. Paragraph 68 of IFRS 15 indicates that the requirements for constraining estimates of variable consideration are applied if the fair value of the non-cash consideration promised by a customer varies for reasons other than only the form of the consideration (for example, a change in the exercise price of a share option because of the entity's performance). The FASB observed that applying the variable consideration requirements to both types of variability might not provide users of financial statements with useful information, because the timing of revenue recognition might differ for similar transactions settled in different forms of consideration (for example, cash and shares). Additionally, the inclusion of a minor performance condition could significantly affect the amount of non-cash consideration that would be subject to the constraint on variable consideration.

BC254H The IASB noted that paragraph BC252 explains that the boards decided to constrain variability in the estimate of the fair value of the non-cash consideration if that variability relates to changes in the fair value for reasons other than the form of the consideration (ie for reasons other than changes in the price of the non-cash consideration). The IASB also noted the view of some TRG members that in practice it might be difficult to distinguish between variability in the fair value due to the form of the consideration and other reasons, in which case applying the variable consideration constraint to the whole of the estimate of the non-cash consideration might be more practical. However, for reasons similar to those discussed in paragraph BC254E, the IASB decided not to amend IFRS 15 for this issue. Consequently, the IASB

acknowledged that differences may arise between an entity reporting under IFRS and an entity reporting under US GAAP.

Consideration payable to a customer (paragraphs 70–72)

- BC255 In some cases, an entity pays consideration to one of its customers or to its customer's customer (for example, an entity may sell a product to a dealer or distributor and subsequently pay a customer of that dealer or distributor). That consideration might be in the form of a payment in exchange for goods or services received from the customer, a discount or refund for goods or services provided to the customer, or a combination of both.
- BC256 To help an entity distinguish between those types of payments, the boards decided that the only circumstance in which an entity should account for any good or service received in the same way as for other purchases from suppliers is if the good or service is distinct. Previous requirements in US GAAP on the consideration that a vendor gives to a customer used the term 'identifiable benefit', which was described as a good or service that is 'sufficiently separable from the recipient's purchase of the vendor's products such that the vendor could have entered into an exchange transaction with a party other than a purchaser of its products or services in order to receive that benefit'. The boards concluded that the principle in IFRS 15 for assessing whether a good or service is distinct is similar to the previous requirements in US GAAP.
- BC257 The amount of consideration received from a customer for goods or services, and the amount of any consideration paid to that customer for goods or services, could be linked even if they are separate events. For instance, a customer may pay more for goods or services from an entity than it would otherwise have paid if it was not receiving a payment from the entity. Consequently, the boards decided that to depict revenue faithfully in those cases, any amount accounted for as a payment to the customer for goods or services received should be limited to the fair value of those goods or services, with any amount in excess of the fair value being recognised as a reduction of the transaction price.
- BC258 If the payment of consideration is accounted for as a reduction of the transaction price, an entity would recognise less revenue when it satisfies the related performance obligation(s). However, in some cases, an entity promises to pay consideration to a customer only after it has satisfied its performance obligations and, therefore, after it has recognised revenue. When this is the case, a reduction in revenue should be recognised immediately. Accordingly, the boards clarified that the reduction of revenue is recognised at the later of when the entity transfers the goods or services to the customer and when the entity promises to pay the consideration. By using the phrase 'promises to pay', the boards clarified that an entity should reflect in the transaction price payments to customers that are conditional on future events (for example, a promise to pay a customer that is conditional on the customer making a specified number of purchases would be reflected in the transaction price when the entity makes the promise).

Customer credit risk

- BC259 The 2010 Exposure Draft proposed that an entity would recognise revenue at the amount that the entity expects to *receive* from the customer. In other words, the customer's credit risk would be reflected in the measurement of the transaction price allocated to the performance obligations in the contract.
- BC260 Many respondents to the 2010 Exposure Draft commented specifically about the proposed requirements for customer credit risk. Although some respondents agreed with the proposal that the transaction price should reflect the customer's credit risk, nearly all respondents (including preparers, users of financial statements and securities regulators) expressed concerns about applying that concept in practice. In particular, many users of financial statements commented that they would prefer revenue to be measured at the 'gross' amount so that revenue growth and receivables management (or bad debts) could be analysed separately. Those users of financial statements indicated that they were interested in assessing the performance of an entity's sales function and receivables collection function separately because those functions are often managed separately. However, that information would not be available if an entity's assessment of sales and collectability were reflected only on a 'net' basis in the revenue line.
- BC261 After considering that feedback, the boards decided not to adopt that proposal. Instead, in the 2011 Exposure Draft, the boards proposed that revenue should be recognised at the amount to which the entity expects to be entitled, which would not reflect any adjustments for amounts that the entity might not be able to collect from the customer. However, to provide transparency to all users of financial statements for the portion of the entity's gross revenue that is expected to be uncollectable, the boards proposed to link the presentation of the revenue line and the impairment loss line. Consequently, the 2011 Exposure Draft proposed that initial and subsequent impairment losses (and reversals) on transactions that did not include a significant financing component should be presented as a separate line item adjacent to the revenue line item.
- BC262 In redeliberating the 2011 Exposure Draft, the boards considered the following challenges arising from the proposed linked presentation of revenue and impairment losses:
- (a) different interpretations might have emerged about whether the reported revenue amount of the entity is the gross revenue before the impairment losses that are presented adjacent to revenue or the net revenue after those impairment losses.
 - (b) the impairment losses that would have been presented as a separate line item adjacent to the revenue line item might have related to uncollectable consideration that had been recognised as revenue in previous reporting periods. Consequently, there would not necessarily be a connection between the revenue recognised in a particular reporting period and the impairment losses that would have been presented adjacent to the revenue line item in that period.

- (c) the impairment losses on short-term trade receivables (ie receivables arising from contracts with customers that do not have separately identified financing components) would have been presented differently from all other financial assets that are subject to impairment. This is because the impairment losses for short-term trade receivables would have been presented adjacent to revenue, whereas for all other financial assets, impairment losses would have been presented together with other expense items in the statement of comprehensive income. For the reasons described in paragraphs BC244–BC247, those other financial assets would have included receivables arising from contracts with customers that include a financing component that is significant to the contract.

BC263 The boards considered addressing some of those challenges by requiring that initial impairment losses be presented adjacent to the revenue line item and subsequent impairment losses be presented as a separate expense. The boards observed that this approach would have provided a clearer link between revenue and the impairment losses related to the revenue recognised in that period. However, many respondents noted that it would have been challenging to distinguish between initial and subsequent impairment losses without incurring significant costs to obtain the information.

BC264 Consequently, the boards decided to modify the presentation requirements for impairment losses and to require disclosure of impairment losses on short-term trade receivables arising from a contract with a customer separate from other impairment losses (if not otherwise presented and subject to the usual materiality considerations). The boards decided that this approach is the most appropriate because it addresses the challenges identified in the 2011 Exposure Draft and still provides users of financial statements with the information that they had said would be most useful, which is gross revenue to provide revenue trend information and the impairment loss to provide information on receivables management (or bad debts). Furthermore, the boards noted that this would provide greater consistency with the accounting for impairment losses on contracts with customers that include a significant financing component.

BC265 However, the boards were concerned that for some transactions in which there is significant credit risk at contract inception, an entity might recognise revenue for the transfer of goods or services and, at the same time, recognise a significant bad debt expense. The boards decided that in those cases, ‘grossing up’ revenue and recognising a significant impairment loss would not faithfully represent the transaction and would not provide useful information. Consequently, the boards included the criterion in paragraph 9(e) of IFRS 15 (see paragraphs BC42–BC46).

Allocating the transaction price to performance obligations (paragraphs 73–86)

- BC266 The boards decided that an entity should generally allocate the transaction price to all performance obligations in proportion to the stand-alone selling prices of the goods or services underlying each of those performance obligations at contract inception (ie on a relative stand-alone selling price basis). They decided that in most cases an allocation based on stand-alone selling prices faithfully depicts the different margins that may apply to promised goods or services.
- BC267 Most respondents agreed with the requirement to allocate the transaction price on a relative stand-alone selling price basis. Some of those respondents observed that the requirements were broadly consistent with previous changes to US GAAP for multiple-element arrangements. However, respondents expressed concerns about the following topics:
- (a) estimating the stand-alone selling price; and
 - (b) allocating discounts and contingent consideration.

Estimating stand-alone selling prices (paragraphs 76–80)

- BC268 IFRS 15 specifies that if an entity does not have an observable price from selling a good or service separately, the entity should instead estimate the stand-alone selling price. Paragraph 79 of IFRS 15 includes examples of suitable estimation methods for estimating the stand-alone selling price. However, the boards decided not to preclude or prescribe any particular method for estimating a stand-alone selling price so long as the estimate is a faithful representation of the price at which the entity would sell the distinct good or service if it were sold separately to the customer. The boards clarified that the method used by the entity to estimate a stand-alone selling price should maximise the use of observable inputs and should be applied consistently to estimate the stand-alone selling price of other goods or services with similar characteristics.
- BC269 The boards observed that many entities may already have robust processes for determining stand-alone selling prices on the basis of reasonably available data points and the effects of market considerations and entity-specific factors. However, other entities may need to develop processes for estimating selling prices of goods or services that are typically not sold separately. The boards decided that when developing those processes, an entity should consider all reasonably available information on the basis of the specific facts and circumstances. That information might include the following:
- (a) reasonably available data points (for example, a stand-alone selling price of the good or service, the costs incurred to manufacture or provide the good or service, related profit margins, published price listings, third-party or industry pricing and the pricing of other goods or services in the same contract);

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- (b) market conditions (for example, supply and demand for the good or service in the market, competition, restrictions and trends);
- (c) entity-specific factors (for example, business pricing strategies and practices); and
- (d) information about the customer or class of customer (for example, type of customer, geographical region and distribution channel).

Residual approach

BC270 In response to questions from respondents, the boards decided to specify that a residual approach might be a suitable technique for estimating the stand-alone selling price of a good or service. Using a residual approach, an entity would estimate a stand-alone selling price of a good or service on the basis of the difference between the total transaction price and the (observable) stand-alone selling prices of other goods or services in the contract.

BC271 The boards also decided to specify how and when an entity can use the residual approach as an estimation method in paragraph 79(c) of IFRS 15. Specifically, in situations in which one or more promised goods or services have a stand-alone selling price that is highly variable or uncertain. In specifying those circumstances, the boards were particularly mindful of the challenges in determining stand-alone selling prices in contracts for intellectual property and other intangible products. In those arrangements, the pricing can be highly variable because there is little or no incremental cost to the entity in providing those goods or services to a customer. In those circumstances, the most reliable way of determining the stand-alone selling price in the contract will often be to use a residual approach. For the same reason, the boards noted that the residual approach might be appropriate in situations in which an entity has not yet established the selling price for a good or service that previously has not been sold on a stand-alone basis.

BC272 Most respondents agreed with the boards' proposals on the residual approach. However, some respondents, particularly those in the software industry, asked the boards to clarify whether they could use a residual approach if there is more than one good or service in the contract with highly variable or uncertain stand-alone selling prices. Those respondents observed that this may occur in contracts that include three or more performance obligations, in which at least one of the performance obligations has an observable stand-alone selling price. The boards decided that even if a contract includes more than one good or service with a highly variable or uncertain stand-alone selling price, an entity should not be prevented from applying the residual approach because it may still be a reliable method for determining the stand-alone selling price. However, the boards observed that using the residual approach when there are two or more goods or services with highly variable or uncertain stand-alone selling prices may require an entity to use a combination of techniques to estimate the stand-alone selling prices as follows:

- (a) apply the residual approach to estimate the aggregate of the stand-alone selling prices for all the promised goods or services with highly variable or uncertain stand-alone selling prices; and
- (b) then use another technique to estimate the stand-alone selling prices of each of those promised goods or services with highly variable or uncertain stand-alone selling prices.

BC273 In determining whether the estimate is reasonable, the boards observed that it was important to understand that the residual approach for estimating the stand-alone selling price of a promised good or service is different from the residual method permitted under previous revenue Standards. This is because in IFRS 15 the residual approach is used to determine the stand-alone selling price of a distinct good or service. By definition, the outcome of this approach cannot realistically result in a stand-alone selling price of zero if the good or service is in fact distinct because to be distinct that good or service must have value on a stand-alone basis. In contrast, the residual method in previous revenue Standards could have resulted in an outcome of zero because the residual method was an allocation method. Thus, under previous revenue recognition requirements, zero could be the only amount of consideration that remained to be allocated to a performance obligation. Consequently, the boards noted that if the residual approach in paragraph 79(c) of IFRS 15 results in no, or very little, consideration being allocated to a good or service or a bundle of goods or services, the entity should consider whether that estimate is appropriate in those circumstances.

Specifying a hierarchy of evidence

BC274 The boards decided not to specify a hierarchy of evidence to determine the stand-alone selling price of a good or service. Instead, they decided to emphasise that an entity should maximise the use of observable inputs when developing estimates of stand-alone selling prices.

BC275 Most respondents agreed with the boards' decision not to prescribe a hierarchy of evidence for estimating a stand-alone selling price. However, some respondents recommended that the boards should specify a hierarchy of evidence, because specifying a hierarchy of evidence for determining stand-alone selling prices (and requiring disclosures using that hierarchy) would enhance the quality and reliability of an entity's reported revenues. The hierarchy suggested by those respondents was similar to that in previous revenue Standards:

- (a) if vendor-specific objective evidence of a selling price is available, an entity would use this price to determine the selling price of a promised good or service;
- (b) if vendor-specific objective evidence is not available, an entity would determine the selling price using third-party evidence, if available; and
- (c) if third-party evidence is not available, an entity would use its best estimate of the selling price.

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BC276 The boards observed that IFRS 15 requires an entity to use observable prices when a good or service is sold separately by the entity (which is similar to a vendor-specific objective evidence notion). It is only when a good or service is not sold separately that an entity is required to estimate the stand-alone selling price. In that estimation process, an entity is still required to maximise the use of observable inputs. The boards noted that in the hierarchy in paragraph BC275 there is little distinction between third-party evidence and a best estimate of a selling price. For instance, third-party evidence of a selling price might require adjustments to reflect differences in either (a) the good or service (because the third-party price could be for a similar, rather than an identical, good or service) or (b) pricing strategies between the third party and the entity. Therefore, the boards affirmed their decision not to specify a hierarchy in IFRS 15. Instead, the boards decided that it was important to emphasise that an entity should maximise the use of observable inputs when developing estimates of stand-alone selling prices.

Allocating discounts and variable consideration (paragraphs 81–86)

BC277 A consequence of allocating the transaction price on a relative stand-alone selling price basis is that any discount in the contract is allocated proportionately to each of the performance obligations in the contract. Some respondents noted that this would not always faithfully depict the amount of consideration to which an entity is entitled for satisfying a particular performance obligation. For example, those respondents noted that the allocation of the discount could result in a loss on one part of the contract although the contract as a whole may be profitable (for example, the contract contains both a high-margin item and a low-margin item). They suggested that the boards should permit an entity to allocate the discount in a contract using one of the following alternatives:

- (a) a management approach, in which an entity would assess which promised good or service is priced at a discount to its stand-alone selling price.
- (b) a residual approach, in which any discount in the contract would be allocated entirely to the satisfied performance obligations.
- (c) a profit margin approach, in which an entity would allocate the discount in a contract in proportion to the individual profit margin on each performance obligation. The individual profit margin for each performance obligation is the difference between the stand-alone selling price and the direct costs of the good or service underlying each performance obligation.

BC278 Another consequence of allocating the transaction price on a relative stand-alone selling price basis is that any amount of consideration that is variable will be allocated to each of the performance obligations in the contract. Some respondents noted that this allocation will not always faithfully depict the amount of consideration to which an entity is entitled upon satisfying a particular performance obligation, if the variable consideration does not relate

to all of the performance obligations in the contract. Many suggested that any adjustment in the transaction price as a result of variable amounts should be allocated only to the performance obligation(s) to which the variable amounts relate.

- BC279 The boards noted that the objective of the revenue recognition model is for an entity to recognise revenue in the amount of consideration to which it expects to be entitled from the customer in exchange for transferring goods or services. The relative stand-alone selling price basis allocation is simply a method to achieve that objective rather than being the allocation principle.
- BC280 However, the boards also noted that allocating the transaction price on a relative stand-alone selling price basis brings rigour and discipline to the process of allocating the transaction price and, therefore, enhances comparability both within an entity and across entities. Consequently, the boards decided that it should be the default method for allocating the transaction price. However, they agreed with respondents that it might not always result in a faithful depiction of the amount of consideration to which the entity expects to be entitled from the customer. Accordingly, in paragraphs 81–86 of IFRS 15, the boards specified the circumstances in which other methods should be used.

Allocating discounts (paragraphs 81–83)

- BC281 IFRS 15 requires an entity to allocate a discount entirely to one or more, but not all, performance obligations in the contract if the entity has observable selling prices for each performance obligation in the contract and those observable stand-alone selling prices provide evidence that the entire discount in the contract is specifically attributable to one or more of those performance obligations. Those requirements are largely based on the ‘contract segmentation’ principle that was included in the 2010 Exposure Draft, which only allowed a discount to be allocated entirely to one or more performance obligations on the basis of goods or services that are priced independently.
- BC282 Some respondents questioned whether the requirements in paragraph 82 of IFRS 15 for allocating a discount are too restrictive and, therefore, might yield outcomes that are inconsistent with the economics of some transactions. However, the boards noted that the requirements are included to maintain the rigour and discipline of a stand-alone selling price allocation and, thus, appropriately restrict the situations in which a discount should not be allocated pro rata to all performance obligations in the contract.
- BC283 The boards also noted that paragraph 82 of IFRS 15 would typically apply to contracts for which there are at least three performance obligations. This is because an entity could demonstrate that a discount relates to two or more performance obligations when it has observable information supporting the stand-alone selling price of a group of those promised goods or services when they are sold together. The boards noted that it may be possible for an entity to have sufficient evidence to be able to allocate a discount to only one performance obligation in accordance with the criteria in paragraph 82, but the boards expected that this could only occur in rare cases.

Allocating variable consideration (paragraphs 84–86)

BC284 The boards agreed with respondents that it would not always be appropriate for an entity to allocate the variable consideration in a transaction price to all of the performance obligations in a contract. For example, an entity may contract to provide two products at different times with a bonus that is contingent on the timely delivery of only the second product. In that example, it might be inappropriate to attribute variable consideration included in the transaction price to both products. Similarly, an entity may contract to provide two products at different times with a fixed amount for the first product that represents that product's stand-alone selling price, and a variable amount that is contingent on the delivery of the second product. That variable amount might be excluded from the estimate of the transaction price (ie because of the requirements for constraining estimates of the transaction price). In that case, it might be inappropriate to attribute the fixed consideration included in the transaction price to both products. Consequently, the boards specified the criteria in paragraphs 84–86 of IFRS 15 to identify the circumstances in which an entity should allocate the variable consideration entirely to a performance obligation or to a distinct good or service (that forms part of a single performance obligation) rather than to the contract as a whole. The boards decided that those criteria are necessary to ensure an appropriate allocation of the transaction price when there is variable consideration in the transaction price.

BC285 The boards clarified in paragraph 84(b) of IFRS 15 that variable consideration can be allocated to distinct goods or services even if those goods or services form a single performance obligation. The boards made this clarification to ensure that an entity can, in some cases, attribute the reassessment of variable consideration to only the satisfied portion of a performance obligation when that performance obligation meets the criterion in paragraph 22(b) of IFRS 15. Consider the example of a contract to provide hotel management services for one year (ie a single performance obligation in accordance with paragraph 22(b) of IFRS 15) in which the consideration is variable and determined based on two per cent of occupancy rates. The entity provides a daily service of management that is distinct and the uncertainty related to the consideration is also resolved on a daily basis when the occupancy occurs. In those circumstances, the boards did not intend for an entity to allocate the variable consideration determined on a daily basis to the entire performance obligation (ie the promise to provide management services over a one-year period). Instead, the variable consideration should be allocated to the distinct service to which the variable consideration relates, which is the daily management service.

Changes in transaction price

BC286 The boards also decided to specify that any subsequent changes in the transaction price should be allocated in a manner that is consistent with the allocation methodology at contract inception. This ensures that changes in the estimate of the variable consideration that are included in (or excluded from) the transaction price are allocated to the performance obligation(s) to which

the variable consideration relates. Consequently, the boards specified in paragraph 89 of IFRS 15 that an entity should allocate a change in the transaction price entirely to one or more distinct goods or services if the criteria in paragraph 85 of IFRS 15 are met.

Contingent revenue cap and the portfolio approach to allocation

- BC287 Some respondents disagreed with the boards' proposal that the transaction price should be allocated on a relative stand-alone selling price basis. Those respondents (primarily from the telecommunications and cable television industries) disagreed because allocating the transaction price using relative stand-alone selling prices on a contract-by-contract basis could be complex and costly for their industries. This is because entities in those industries:
- (a) have a high volume of contracts with various potential configurations;
 - (b) provide multiple goods and services in those contracts;
 - (c) include a discount in the contracts; and
 - (d) provide the goods or services at different times.
- BC288 Those respondents also disagreed with allocating the transaction price on the basis of relative stand-alone selling prices because it would provide a revenue recognition pattern that they considered would not be useful to users of their financial statements.
- BC289 Those respondents requested that the boards should carry forward previous revenue recognition requirements in US GAAP (previously referred to as 'the contingent revenue cap'). Those requirements were previously used by many telecommunications entities applying US GAAP and IFRS. In the respondents' view, carrying forward those requirements would have simplified the application of the revenue recognition model by limiting the amount of consideration that a telecommunications entity could allocate to a handset that is bundled with network services to the amount that is not contingent on the delivery of network services in the future. Consequently, revenue would have been recognised at the amount that the customer paid for the handset at contract inception when the handset was transferred to the customer. The remaining contractual payments would have been recognised subsequently as revenue as the entity provided network services to the customer. Many users of financial statements of entities in the telecommunications industry agreed that this revenue recognition pattern would have been useful because it closely relates to the timing of cash received.
- BC290 Respondents from the telecommunications industry commented that without a contingent revenue cap, not only will the application of the revenue recognition model be complex, but revenue will also be recognised for delivering a handset in an amount that exceeds the amount of consideration paid for the handset. In their view, this is inappropriate because it will not be useful to users of their financial statements and, in a separate objection, because they will be entitled to collect the excess only when they provide the network services. Consequently, they reasoned that the contract asset that

will result from recognising revenue for delivery of the handset will not meet the definition of an asset. In addition, they suggested that without a contingent revenue cap, the model will be complex and costly to apply because of the high volume of contracts that they will have to manage and the various potential configurations of handsets and network service plans.

BC291 However, the boards decided not to carry forward the contingent revenue cap for the following reasons:

- (a) limiting the amount of consideration that can be allocated to a satisfied performance obligation is tantamount to cash-basis accounting and does not meet the core principle of IFRS 15. This is because revenue recognised would not depict the amount of consideration to which an entity expects to be entitled for the delivered good or service. Consequently, the contingent revenue cap could result in economically similar contracts being accounted for differently.
- (b) the contingent revenue cap can result in the recognition of losses if the contract is profitable. That would occur if the amount allocated to a satisfied performance obligation is limited to an amount (potentially to zero) that is less than the expenses recognised for the costs of providing the good or service (unless those costs are deferred). However, costs relating to a good or service already transferred to a customer would not give rise to an asset.
- (c) recognising a contract asset in the situation described in paragraph BC290 is appropriate because the entity has a valuable contractual right as a result of satisfying a performance obligation and that right meets the definition of an asset. That right exists even if the entity does not have the unconditional right to collect consideration from the customer. This is because if the entity were to transfer the remaining rights and performance obligations in the contract to a third party after it had delivered a handset, it would expect to be compensated for that past performance.
- (d) applying the contingent cap more broadly than it was applied in previous revenue Standards could have had far-reaching consequences. For example, in many service contracts (including construction contracts), it is appropriate to recognise revenue when services are provided even though the amount of consideration is contingent on the entity's future performance. Otherwise, the entity would not recognise any revenue until reaching a contract milestone or potentially until completion of the contract (which would not depict the transfer of goods or services to the customer).
- (e) although the consequences for construction and other service contracts could have been reduced by limiting the amount allocated to satisfied performance obligations (rather than limiting the amount allocated to a satisfied portion of a single performance obligation), the boards decided that this would have created an arbitrary distinction

and would have put additional pressure on the criteria for identifying performance obligations.

- (f) for many contracts that were previously accounted for under the contingent revenue cap, the amount of consideration allocated to delivered items was not contingent because, even if the customer cancelled the contract, the customer would have been obliged to pay for the delivered item(s). For example, in some contracts for the sale of a handset and network services, either the contract was not cancellable or, if it was, the customer was obliged to pay a termination fee that corresponded with the value of the handset that was delivered upfront (even if the entity might choose not to enforce payment of that fee).

BC292 In addition, the boards decided not to introduce an exception to the revenue recognition model for telecommunications and similar contracts because they do not view those contracts as being different from other contracts in which an entity transfers a bundle of goods or services. Furthermore, the boards decided that IFRS 15 provides a more consistent basis for recognising revenue and produces results in accounting that more closely match the underlying economics of transactions.

BC293 The boards also observed that entities in the telecommunications industry may be able to simplify the application of the model by using portfolio techniques (as envisioned by the practical expedient specified in paragraph 4 of IFRS 15) to allocate the transaction price for a group of similar contracts (see paragraphs BC69–BC70). The boards considered whether they should provide more specific guidance as to when an entity could use a portfolio approach for allocating the transaction price. However, the boards decided not to do so because they were concerned that any further guidance (for example, by including criteria that an entity would need to meet to apply a portfolio approach) might make the practical expedient less useful across entities or jurisdictions.

Onerous performance obligations

BC294 In the 2010 and the 2011 Exposure Drafts, the boards proposed including requirements for identifying and measuring onerous performance obligations in contracts with customers (ie an ‘onerous test’). In those proposals, the boards concluded that an onerous test was needed because the initial measurements of performance obligations are not routinely updated. In addition, the boards noted that including an onerous test would achieve greater convergence of IFRS and US GAAP.

BC295 However, many respondents to the 2010 and the 2011 Exposure Drafts disagreed with the onerous test and highlighted a number of practical application difficulties. Furthermore, many explained that strict application of the onerous test would have resulted in recognition of liabilities in cases in which the outcome of fulfilling a single performance obligation was onerous but the outcome of fulfilling the entire contract would be profitable. A number of respondents suggested removing the onerous test from the revenue proposals because, in addition to being complex and difficult to apply, the

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requirements for recognition of onerous losses are already sufficiently addressed in other Standards. Those respondents commented that:

- (a) for IFRS, the onerous test in IAS 37 and the requirements in IAS 2 *Inventories* already provide sufficient guidance for determining when to recognise losses arising from contracts with customers.
- (b) for US GAAP, existing requirements for recognition of losses from contracts are adequate and if a change to those requirements is necessary, that change could instead be handled in a separate project that addresses liabilities in Topic 450.

BC296 The boards agreed that existing requirements in both IFRS and US GAAP could adequately identify onerous contracts. Furthermore, the boards noted that although their existing requirements for onerous contracts are not identical, they are not aware of any pressing practice issues resulting from the application of those existing requirements. Consequently, the boards decided that IFRS 15 should not include an onerous test. Instead, entities applying IFRS or US GAAP will use their respective existing requirements for the identification and measurement of onerous contracts.

Contract costs (paragraphs 91–104)

Incremental costs of obtaining a contract (paragraphs 91–94)

BC297 The boards decided that an entity should recognise as an asset the incremental costs of obtaining a contract with a customer if the entity expects to recover those costs. The boards defined the incremental costs of obtaining a contract as the costs that an entity incurs in its efforts to obtain a contract that would not have been incurred if the contract had not been obtained. The boards acknowledged that, in some cases, an entity's efforts to recognise an asset from incremental acquisition costs might exceed the financial reporting benefits. Consequently, as a practical expedient, the boards decided to allow an entity to recognise those costs as expenses when incurred for contracts in which the amortisation period for the asset that the entity otherwise would have recognised is one year or less.

BC298 The boards considered requiring an entity to recognise all of the costs of obtaining a contract as expenses when those costs are incurred. The boards observed that, conceptually, an entity may obtain a contract asset as a result of its efforts to obtain a contract (because the measure of the remaining rights might exceed the measure of the remaining obligations). However, because the principle in IFRS 15 requires an entity to recognise a contract asset and revenue only as a result of satisfying a performance obligation in the contract, the boards observed that on the basis of that reasoning, the contract asset would be measured at zero at contract inception and any costs of obtaining a contract would therefore be recognised as expenses when incurred.

- BC299 Many respondents disagreed with recognising all costs to obtain a contract as expenses when incurred because those costs meet the definition of an asset in some cases. In addition, they noted the following:
- (a) other Standards require some of the costs of obtaining a contract to be included in the carrying amount of an asset on initial recognition; and
 - (b) the recognition of the costs of obtaining a contract as expenses would be inconsistent with the tentative decisions in the boards' projects on leases and insurance contracts.
- BC300 During the redeliberations, the boards decided that, in some cases, it might be misleading for an entity to recognise all the costs of obtaining a contract as expenses, when incurred. For example, the boards observed that recognising the full amount of a sales commission as an expense at inception of a long-term service contract (when that sales commission is reflected in the pricing of that contract and is expected to be recovered) would fail to acknowledge the existence of an asset.
- BC301 Consequently, the boards decided that an entity would recognise an asset from the costs of obtaining a contract and would present the asset separately from the contract asset or the contract liability. To limit the acquisition costs to those that can be clearly identified as relating specifically to a contract, the boards decided that only the incremental costs of obtaining a contract should be included in the measurement of the asset, if the entity expects to recover those costs. The boards decided that determining whether other costs relate to a contract is too subjective.
- BC302 The boards noted that it might be difficult for some entities to determine whether a commission payment is incremental to obtaining a new contract (for example, payment of a commission might depend on the entity successfully acquiring several contracts). The boards considered whether to allow an accounting policy election for contract costs, under which an entity would have been able to choose to recognise an asset from the acquisition costs or recognise those costs as an expense (with disclosure of the accounting policy election). The boards noted that this would have been consistent with previous revenue recognition requirements in US GAAP for public entities. However, the boards noted that introducing accounting policy elections into IFRS 15 would have reduced comparability and therefore would not have met one of the key objectives of the Revenue Recognition project to improve comparability in accounting among entities and industries. Consequently, the boards decided not to allow entities an accounting policy election with respect to contract acquisition costs.
- BC303 The FASB noted that depending on the specific facts and circumstances of the arrangement between an asset manager and the other parties in the relationship, the application of the requirements for incremental costs of obtaining a contract might have resulted in different accounting for sales commissions paid to third-party brokers (ie in some cases the commission would have been recognised as an asset while in others it would have been recognised as an expense). The FASB observed that it had not intended the application of the cost requirements to result in an outcome for these specific

types of sales commissions that would be different from applying existing US GAAP. Consequently, the FASB decided to retain the specific cost requirements for investment companies in paragraph 946-605-25-8 of the Codification which has been moved to Subtopic 946-720 *Financial Services – Investment Companies – Other Expenses*.

Costs to fulfil a contract (paragraphs 95–98)

- BC304 The boards developed requirements for accounting for some costs to fulfil a contract. Those requirements were developed in response to concerns that the proposals in the Discussion Paper focused on how an entity should recognise revenue in a contract without considering how the entity should account for the costs to fulfil a contract. Some respondents, particularly those from the construction industry, said that requirements for profit margin recognition are as important as requirements for revenue recognition. Other respondents, mainly preparers who apply US GAAP, were concerned about the withdrawal of requirements for costs that were developed specifically for their own industries.
- BC305 The cost requirements in IFRS 15 are intended to achieve the following:
- (a) fill the gap arising from the withdrawal of previous revenue Standards – IFRS 15 will result in the withdrawal of some requirements for contract costs, in particular, the previous requirements for accounting for construction contracts.
 - (b) improve current practice—the cost requirements provide clearer requirements for accounting for some costs to fulfil a contract (for example, setup costs for services) and result in an entity no longer having to rely on, or analogise to, requirements that were not developed specifically for contracts with customers. For instance, in accounting for setup costs, an entity applying US GAAP may previously have needed to analogise to the guidance on the deferral of direct loan origination costs in paragraph 310-20-25-2 of the Codification. An entity applying IFRS may have evaluated those costs in accordance with IAS 38 *Intangible Assets*. Specifying clear requirements will also result in greater consistency in practice.
 - (c) promote convergence in accounting for contract costs – more costs will be accounted for similarly under IFRS and US GAAP (although total consistency in accounting for costs to fulfil a contract will not be achieved unless the boards align their respective Standards on inventories; property, plant and equipment; intangible assets and impairment of assets).
- BC306 Most respondents supported the boards' inclusion of requirements that address some of the costs to fulfil a contract. Some respondents recommended that the boards address cost requirements comprehensively in a separate project. However, because cost requirements are included in many Standards (such as the ones described in paragraph BC305(c)), the boards noted that this would require reconsideration of those Standards and, therefore, decided against broadening the scope of the cost requirements.

- BC307 Because the boards decided not to reconsider all cost requirements comprehensively, paragraphs 91–98 of IFRS 15 specify the accounting for contract costs that are not within the scope of other Standards. Consequently, if the other Standards preclude the recognition of any asset arising from a particular cost, an asset cannot then be recognised under IFRS 15 (for example, in IFRS, initial operating losses, such as those incurred while demand for an item builds, will continue to be accounted for in accordance with paragraph 20(b) of IAS 16 and, in US GAAP, pre-production costs under long-term supply arrangements will continue to be accounted for in accordance with paragraphs 340-10-25-5 through 25-8 of the Codification).
- BC308 IFRS 15 clarifies that only costs that give rise to resources that will be used in satisfying performance obligations in the future and that are expected to be recovered are eligible for recognition as assets. Those requirements ensure that only costs that meet the definition of an asset are recognised as such and that an entity is precluded from deferring costs merely to normalise profit margins throughout a contract by allocating revenue and costs evenly over the life of the contract. To provide a clear objective for recognising and measuring an asset arising from the costs to fulfil a contract, the boards decided that only costs that relate directly to a contract should be included in the cost of the asset.

Amortisation and impairment (paragraphs 99–104)

- BC309 The boards decided that an entity should amortise the asset recognised from the costs of obtaining and fulfilling a contract in accordance with the pattern of transfer of goods or services to which the asset relates. Respondents broadly agreed; however, some asked the boards to clarify whether those goods or services could relate to future contracts. Consequently, the boards clarified that in amortising the asset in accordance with the transfer of goods or services to which the asset relates, those goods or services could be provided under a specifically anticipated (ie future) contract. That conclusion is consistent with the notion of amortising an asset over its useful life and with other Standards. However, amortising the asset over a longer period than the initial contract would not be appropriate in situations in which an entity pays a commission on a contract renewal that is commensurate with the commission paid on the initial contract. In that case, the acquisition costs from the initial contract do not relate to the subsequent contract.
- BC310 The boards considered testing a recognised asset arising from fulfilment costs for impairment using one of the existing impairment tests in their respective requirements (for example, IAS 2 and IAS 36 *Impairment of Assets* or Topic 330 *Inventory*, Topic 360 *Property, Plant and Equipment* and Subtopic 985-20 *Software – Costs of Software to Be Sold, Leased, or Marketed*). However, the boards decided that an entity should consider only the economic benefits in the contract with the customer and, consequently, the impairment test should be based on comparing the carrying amount of the asset with the remaining amount of promised consideration in exchange for the goods or services to which the asset relates, less the remaining costs of providing those goods or services. The boards decided that for purposes of impairment testing, the entity should

consider future cash flows that may be too uncertain to include in the recognition of revenue (see paragraphs BC203–BC223). The boards decided this because their objective for measuring and recognising impairments of contract acquisition and fulfilment costs is different from the measurement objective for revenue. The impairment objective is to determine whether the carrying amount of the contract acquisition and fulfilment costs asset is recoverable. Consequently, the measurement objective is consistent with other impairment methods in IFRS and US GAAP that include an assessment of customer credit risk and expectations of whether amounts of variable consideration will be received.

- BC311 The FASB decided that an entity should not reverse an impairment charge when the reasons for the impairment no longer exist. Conversely, the IASB decided that the impairment charge should be reversed in those circumstances under IFRS. The boards acknowledged that this would result in entities accounting differently for those contract costs using IFRS and US GAAP. However, the boards decided that it is important for the requirements to be consistent with their respective impairment models for other types of assets and those impairment models differ in their accounting for reversals of impairments.

Learning curve

- BC312 A 'learning curve' is the effect of efficiencies realised over time when an entity's costs of performing a task (or producing a unit) decline in relation to how many times the entity performs that task (or produces that unit). The phenomenon of a learning curve can exist independently of a contract with a customer. For example, a typical manufacturer that produces units of inventory would become more efficient in its production process over time. Some respondents asked how to apply the proposals to account for the effects of learning costs in a contract with a customer.
- BC313 The boards noted that IFRS 15 addresses the accounting for the effects of learning costs if both of the following conditions are satisfied:
- (a) an entity has a single performance obligation to deliver a specified number of units; and
 - (b) the performance obligation is satisfied over time.
- BC314 In that situation, an entity recognises revenue by selecting a method of measuring progress that depicts the transfer over time of the good or service to the customer. An entity would probably select a method (for example, cost-to-cost) that results in the entity recognising more revenue and expense for the early units produced relative to the later units. That effect is appropriate because of the greater value of the entity's performance in the early part of the contract because, if an entity were to sell only one unit, it would charge the customer a higher price for that unit than the average unit price the customer pays when the customer purchases more than one unit.

- BC315 In other situations, an entity may promise to deliver a specified number of units in a contract, but that promise does not give rise to a single performance obligation that is satisfied over time. The boards decided that, in those situations, an entity should apply the requirements of other Standards (for example, IAS 2) for the following reasons:
- (a) if an entity incurs costs to fulfil a contract without also satisfying a performance obligation over time, the entity probably would be creating an asset included within the scope of other Standards (for example, the costs of producing tangible units would accumulate as inventory, and the entity would select an appropriate method of measuring that inventory). In those cases, the boards decided that an entity should not account for the learning curve differently depending on whether or not a contract exists.
 - (b) the type of contract described in this paragraph is not the type of contract typically entered into by respondents who asked how the requirements of IFRS 15 would apply to learning curve effects (in most cases, those respondents enter into contracts that would be accounted for as a performance obligation satisfied over time).
- BC316 The boards, however, acknowledged the diversity in practice when accounting (in accordance with other Standards) for the costs of products produced under long-term production programmes, but agreed that they could not address these matters as part of the Revenue Recognition project.

Presentation (paragraphs 105–109)

- BC317 The boards decided that the remaining rights and performance obligations in a contract should be accounted for and presented on a net basis, as either a contract asset or a contract liability. The boards noted that the rights and obligations in a contract with a customer are interdependent—the right to receive consideration from a customer depends on the entity’s performance and, similarly, the entity performs only as long as the customer continues to pay. The boards decided that those interdependencies are best reflected by accounting and presenting on a net basis the remaining rights and obligations in the statement of financial position.
- BC318 The boards considered whether the rights and performance obligations in contracts that are subject to the legal remedy of specific performance should be presented on a gross basis, that is, as separate assets and liabilities. The boards observed that in the event of a breach of contract, some contracts require the entity and the customer to perform as specified in the contract. Consequently, unlike most contracts that can be settled net, specific performance contracts generally result in a two-way flow of resources between the customer and the entity. Specific performance contracts are akin to financial contracts that are settled by physical delivery rather than by a net cash payment and for which the units of account are the individual assets and liabilities arising from the contractual rights and obligations.

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- BC319 However, the boards decided against making an exception for specific performance contracts. This is because the remedy of specific performance is relatively rare and is not available in all jurisdictions. In addition, it is only one of a number of possible remedies that could be awarded by a court if legal action were taken for breach of contract.
- BC320 The boards decided that IFRS 15 should not specify whether an entity is required to present its contract assets and contract liabilities as separate line items in the statement of financial position. Instead, an entity should apply the general principles for the presentation of financial statements to determine whether to present contract assets and contract liabilities separately in the statement of financial position. For example, IAS 1 *Presentation of Financial Statements* requires an entity to present separately each class of similar items and items of a dissimilar nature or function unless they are immaterial.
- BC321 The boards also observed that some industries have historically used different labels to describe contract assets and contract liabilities or may recognise them in more than one line item either in the financial statements or in the notes. Because that additional detail is often useful to users of those financial statements, the boards decided that an entity could use different descriptions of contract assets, contract liabilities and receivables, and could use additional line items to present those assets and liabilities if the entity also provides sufficient information for users of financial statements to be able to distinguish them.

Relationship between contract assets and receivables

- BC322 When an entity performs first by satisfying a performance obligation before a customer performs by paying the consideration, the entity has a contract asset – a right to consideration from the customer in exchange for goods or services transferred to the customer.
- BC323 In many cases, that contract asset is an unconditional right to consideration – a receivable – because only the passage of time is required before payment of that consideration is due. However, in other cases, an entity satisfies a performance obligation but does not have an unconditional right to consideration, for example, because it first needs to satisfy another performance obligation in the contract. The boards decided that when an entity satisfies a performance obligation but does not have an unconditional right to consideration, an entity should recognise a contract asset in accordance with IFRS 15. The boards noted that making the distinction between a contract asset and a receivable is important because doing so provides users of financial statements with relevant information about the risks associated with the entity's rights in a contract. That is because although both would be subject to credit risk, a contract asset is also subject to other risks, for example, performance risk.

- BC324 Once an entity has an unconditional right to consideration, it should present that right as a receivable separately from the contract asset and account for it in accordance with other requirements (for example, IFRS 9 or Topic 310). The boards decided that IFRS 15 need not address the accounting for receivables in addition to revenue recognition. Issues such as the measurement (or impairment) of receivables and disclosures relating to those assets are already addressed in IFRS and US GAAP.
- BC325 In many cases, an unconditional right to consideration arises when the entity satisfies the performance obligation and invoices the customer. For example, a payment for goods or services is typically due and an invoice is issued when the entity has transferred the goods or services to the customer. However, the act of invoicing the customer for payment does not indicate whether the entity has an unconditional right to consideration. For instance, the entity may have an unconditional right to consideration before it invoices (unbilled receivable) if only the passage of time is required before payment of that consideration is due. In other cases, an entity can have an unconditional right to consideration before it has satisfied a performance obligation. For example, an entity may enter into a non-cancellable contract that requires the customer to pay the consideration a month before the entity provides goods or services. In those cases, on the date when payment is due, the entity has an unconditional right to consideration. (However, in those cases, the entity should recognise revenue only after it transfers the goods or services.)
- BC326 The boards observed that in some cases, an entity will have an unconditional right to consideration, even though the entity may be required to refund some or all of that consideration in the future. In those cases, the possible obligation to refund consideration in the future will not affect the entity's present right to be entitled to the gross amount of consideration. In those cases, the boards observed that an entity may recognise a receivable and a refund liability (for example, when a right of return exists).

Disclosure (paragraphs 110–129)

- BC327 Some of the main criticisms from regulators and users of financial statements about prior revenue Standards in IFRS and US GAAP related to the disclosure requirements. Broadly, regulators and users of financial statements found the disclosure requirements to be inadequate and lacking cohesion with the disclosure of other items in the financial statements. This lack of cohesion made it difficult to understand an entity's revenues, as well as the judgements and estimates made by the entity in recognising those revenues. For example, many users of financial statements observed that entities presented revenue in isolation, with the result that users of financial statements could not relate revenue to the entity's financial position. Consequently, one of the boards' goals in undertaking the Revenue Recognition project was to provide users of financial statements with more useful information through improved disclosure requirements. Many respondents broadly supported that goal. However, respondents' views about the proposed disclosure requirements in the 2011 Exposure Draft were polarised—users of financial statements supported the proposed disclosure requirements because those requirements

would have been a significant improvement over previous requirements. In contrast, other respondents (primarily preparers) noted that, when viewed as a whole, the proposed disclosure requirements would have resulted in voluminous disclosures and they questioned whether the proposed disclosures were justifiable on a cost-benefit basis.

BC328 Because of those polarised views, the boards held workshops with users of financial statements and preparers between September and December 2012 in London (United Kingdom), Tokyo (Japan), and Norwalk and New York City (United States). The objective of those workshops was to discuss issues on disclosure and transition and to identify potential solutions to address both users' needs for useful information and preparers' concerns about the costs of providing that information. As a result of the feedback provided through workshops, other outreach efforts and the comment letters, the boards refined the disclosure requirements proposed in the 2011 Exposure Draft. Those refinements and the reasons for the boards' decisions are explained in paragraphs BC330–BC361.

BC329 The boards noted that the disclosure requirements in paragraphs 110–129 of IFRS 15 are comprehensive and represent a significant improvement from previous requirements. Some may observe that the overall volume of disclosure has increased compared with previous revenue disclosure requirements. However, the boards observed that, to some extent, concerns about the increased volume were the inevitable consequence of addressing the shortcoming in the previous disclosure requirements. In addition, the boards noted that many entities provide voluntary revenue disclosures outside the financial statements and the boards concluded that the increase in disclosure is necessary to improve previous disclosure practices and the usefulness of financial reporting.

Disclosure objective and materiality (paragraphs 110–112)

BC330 The boards decided that, consistently with other recent Standards, IFRS 15 should specify an objective for the revenue disclosures. In the boards' view, a clear objective improves the interpretation and implementation of the disclosure requirements. This is because a preparer can assess whether the overall quality and informational value of its revenue disclosures are sufficient to meet the stated objectives. The boards also observed that specifying an overall disclosure objective avoids the need for detailed and prescriptive disclosure requirements to accommodate the many and varied types of contracts with customers that are within the scope of IFRS 15.

BC331 The boards also decided to include disclosure requirements to help an entity meet the disclosure objective. However, those disclosures should not be viewed as a checklist of minimum disclosures, because some disclosures may be relevant for some entities or industries but may be irrelevant for others. The boards also observed that it is important for an entity to consider the disclosures together with the disclosure objective and materiality. Consequently, paragraph 111 of IFRS 15 clarifies that an entity need not disclose information that is immaterial.

Contracts with customers

- BC332 To provide context for the disclosures, the boards decided to require an entity to disclose the amount of revenue recognised from contracts with customers. The FASB noted that in the absence of a general financial statement presentation standard, it would require an entity to present or disclose the amount of revenue recognised from contracts with customers. However, the IASB noted that the general principles of IAS 1 would apply and, therefore, an entity would need to disclose the amount of revenue recognised from contracts with customers in the notes to the financial statements only if it was not otherwise presented.
- BC333 In addition to the amount of revenue recognised, the boards also decided to require an entity to disclose impairment losses from contracts with customers (if not presented in the statement of comprehensive income). The boards made this decision as a consequence of their previous decisions not to reflect customer credit risk in the measurement of the transaction price and, therefore, the amount of revenue recognised for transactions that do not include a significant financing component (see paragraphs BC259–BC265). This is reflected in the core principle of IFRS 15 that specifies that an entity recognise revenue at an amount that reflects the consideration to which the entity expects to be entitled.
- BC334 In the light of those decisions, the boards decided that separately disclosing (or presenting) the impairment losses on contracts with customers provides the most relevant information to users of financial statements.

Disaggregation of revenue (paragraphs 114–115)

- BC335 Revenue recognised in the statement of comprehensive income is a composite amount arising from many contracts with customers. This is because revenue can arise from the transfer of different goods or services and from contracts that involve different types of customers or markets. Users of financial statements explained that understanding those differences was critical to their analyses. Consequently, the boards decided to require an entity to provide disaggregated revenue information to help users of financial statements understand the composition of the revenue from contracts with customers recognised in the current period.
- BC336 In developing the requirements for disclosing disaggregated revenue, the boards observed that some previous revenue recognition requirements required revenue to be disaggregated into its significant categories, including revenue arising from goods or services. However, because the most useful disaggregation of revenue depends on various entity-specific or industry-specific factors, the boards decided that IFRS 15 should not prescribe any specific factor to be used as the basis for disaggregating revenue from contracts with customers. Instead, the boards decided to specify in paragraph 114 of IFRS 15 an objective for providing disaggregated information. The boards noted that specifying an objective will result in the most useful information for users of financial statements, because it enables an entity to disaggregate revenue into categories that are meaningful for its

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business. In addition, specifying an objective should result in disaggregation that is neither too aggregated nor too detailed.

- BC337 The boards also decided to provide application guidance because of requests for additional guidance about how to implement the objective and, in particular, how to determine the appropriate categories that an entity may use to disaggregate revenue from contracts with customers. The application guidance explains that the most appropriate categories depend on facts and circumstances; however, an entity should consider how revenue is disaggregated in other communications or for the purposes of evaluating financial performance. This is because entities often already disaggregate revenue in those communications and the categories used may be those that are most useful for users of financial statements and that meet the objective in paragraph 114 of IFRS 15. The application guidance also includes a list of examples of categories (for example, geographical region or product type) by which an entity might disaggregate its revenue. The boards noted that the list of categories was compiled as examples that could be applied to many different entities, industries and contracts. As a result, the list should not be viewed either as a checklist or as an exhaustive list. However, the boards observed that an entity may need to disaggregate by more than one category to meet the objective.
- BC338 The boards also decided to require that an entity explain the relationship between the disaggregated revenue information required by paragraph 114 of IFRS 15 and the segment information required by IFRS 8 *Operating Segments* and Topic 280 *Segment Reporting*. The boards decided this because users of financial statements explained that it is critical to their analyses to understand not only the composition of revenue, but also how that revenue relates to other information provided in segment disclosures such as costs of goods sold, expenses and assets used.
- BC339 In developing the requirements, the boards also considered whether the current segment reporting requirements in IFRS 8 and Topic 280 provided adequate information for users of financial statements in understanding the composition of revenue. Those requirements require an entity to disaggregate and disclose revenue for each operating segment (reconciled to total revenue). In addition, those requirements also require an entity to disaggregate total revenue by products or services (or by groups of similar products or services) and geographical areas – if the entity’s operating segments are not based on those factors.
- BC340 However, despite some similarity to segment reporting, the boards decided to require disaggregated revenue information for revenue from contracts with customers in IFRS 15 because some entities are exempt from providing segment disclosures (for example, entities that are not listed on a public stock exchange). Furthermore, the boards observed that segment information might be based on non-GAAP information (ie the revenue that is reported to the chief operating decision maker may be recognised and measured on a basis that is not in accordance with IFRS 15). The boards also observed that the objective of providing segment information in accordance with IFRS 8 or Topic 280 is different from the objective for the disaggregation disclosure in

IFRS 15 and, therefore, segment revenue disclosures may not always provide users of financial statements with enough information to help them understand the composition of revenue recognised in the period. Nonetheless, the boards clarified in paragraph 112 of IFRS 15 that an entity does not need to provide disaggregated revenue disclosures if the information about revenue provided in accordance with IFRS 8 or Topic 280 meets the requirements specified in paragraph 114 of IFRS 15 and those revenue disclosures are based on the recognition and measurement requirements in IFRS 15.

Contract balances (paragraphs 116–118)

- BC341 Users of financial statements explained that they need to understand the relationship between the revenue recognised in a reporting period and the changes in the balances of the entity's contract assets and contract liabilities (ie contract balances) to assess the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. Those users of financial statements noted that even though many entities currently recognise working capital balances such as unbilled receivables and deferred revenue, previous revenue recognition requirements did not require adequate disclosure about the relationship between those balances and the amount of revenue recognised. Consequently, the 2010 and the 2011 Exposure Drafts proposed that an entity disclose a reconciliation of the contract asset and the contract liability balances in a tabular format.
- BC342 However, many preparers strongly opposed any requirements to reconcile the contract asset and the contract liability balances in a tabular format. Those preparers noted that it would be costly to compile and present the information because it was not tracked. Preparers also questioned the usefulness of this reconciliation to users of financial statements, because the information was not used by management. In contrast, users of financial statements reiterated that some of the information in the reconciliation would be useful, including the information about contract liabilities, which would provide greater transparency about future revenues, which is critical to their analyses. However, users of financial statements also acknowledged that the rigid format of the proposed reconciliation had limitations that would have reduced its usefulness. This is because, for example, changes in contract assets and contract liabilities would have been disclosed on an aggregate basis (ie changes in contract assets would have been offset by changes in contract liabilities) and, therefore, the extent of the changes in contract balances (and the reasons for those changes) would have been obscured.
- BC343 In the discussion at the disclosure and transition workshops in 2012 (see paragraph BC328), preparers agreed that they could provide further information about contract balances that would be useful to users of financial statements. However, to limit the costs of providing that information, those preparers explained that they need greater flexibility in the format of this disclosure. Users of financial statements emphasised that it was critical to them to have information on the movements in the contract balances presented separately because it would help them understand information about the following:

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- (a) the amount of the opening balance of the contract liability balance that will be recognised as revenue during the period; and
- (b) the amount of the opening balance of the contract asset that will be transferred to accounts receivable or collected in cash during the period.

BC344 Before addressing concerns about format, the boards considered whether they could address the cost concerns of preparers by limiting the scope of the reconciliation requirements to only contract balances for specific types of contracts (for example, long-term contracts). They did this because many users of financial statements observed that information about contract balances would be particularly important for entities that enter into long-term contracts with customers or that carry significant contract liability balances for other reasons (for example, prepaid service contracts). However, the boards rejected this alternative for the following reasons:

- (a) it would have been difficult to clearly identify the types of contracts or industries for which a reconciliation would (or would not) provide useful information.
- (b) limiting the scope of the reconciliation would have added complexity. This is because limiting the scope could have resulted in excluding some of an entity's contract assets and contract liabilities from the reconciliation and, therefore, additional information would have been required to relate the reconciled amounts of contract assets or contract liabilities to those recognised in the statement of financial position.
- (c) information on contract balances is useful for other contracts, in addition to long-term contracts, because, for example, there may be a number of contracts or businesses that have significant timing differences between payment and performance.

BC345 In the light of their decision not to limit the scope of the disclosure, the boards considered whether they could instead modify the format of the disclosure to address the concerns of preparers and users of financial statements. The boards observed that neither users of financial statements nor preparers supported the format proposed in the 2010 and the 2011 Exposure Drafts because users of financial statements were concerned that the information about the movements in the contract balances was too aggregated to be useful and because preparers were concerned about the cost of compliance with such a rigid format. The boards acknowledged that a previously rejected alternative format of a gross reconciliation of contract balances (ie to show the remaining contractual rights and performance obligations in separate columns) would have been inappropriate because it would not respond to preparers' concerns about costs. This is because the cost of preparing and auditing the gross reconciliation would have been high, and possibly higher than the 'net' reconciliation proposed in the 2011 Exposure Draft, because an entity would have been required to measure all unperformed contracts which would have required a high level of judgement.

- BC346 Consequently, the boards decided that, instead of requiring a tabular reconciliation of the aggregate contract balances, they would require an entity to disclose qualitative and quantitative information about the entity's contract balances (see paragraphs 116–118 of IFRS 15). This approach balances the needs of users of financial statements with preparers' concerns because the qualitative and quantitative disclosures provide users of financial statements with the information they requested (ie information on when contract assets are typically transferred to accounts receivable or collected as cash and when contract liabilities are recognised as revenue). In addition, the boards decided that those disclosures would be more cost-effective than a reconciliation. The boards also observed that this approach would not result in a significant change for many entities that are already disclosing similar information. For example, the boards observed that some long-term construction entities already disclosed information relating to balances similar to contract assets and contract liabilities – often referred to as 'due from customers' or 'unbilled accounts receivable' and 'due to customers' or 'deferred revenue'.
- BC347 The boards also decided to require that an entity disclose the amount of revenue recognised in the period that relates to amounts allocated to performance obligations that were satisfied (or partially satisfied) in previous periods (for example, as a result of a change in transaction price or estimates related to the constraint on revenue recognised). Disclosing those amounts provides relevant information about the timing of revenue recognition that was not a result of performance in the current period and thus provides useful information about the current period operating results and on predicting future revenues. In addition, the boards noted that this information is not provided elsewhere in the financial statements. Finally, the boards noted that, consistent with general materiality requirements, they did not expect this disclosure to be provided if the amounts are immaterial.

Disclosure of the transaction price allocated to the remaining performance obligations (paragraphs 120–122)

- BC348 Many users of financial statements explained that information about the amount and timing of revenue that the entity expects to recognise from its existing contracts would be useful in their analyses of revenue. They also explained that the information would be most useful for long-term contracts, because those contracts typically have the most significant amounts of unrecognised revenue.
- BC349 The boards observed that a number of entities often voluntarily disclose information about their long-term contracts, which is commonly referred to as 'backlog' information. (Some entities are also required to produce this information outside the financial statements in regulatory filings.) However, this information is typically presented outside the financial statements and may not be comparable across entities because there is not a common definition of backlog.

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BC350 In the light of those factors, the boards decided to specify disclosure requirements to capture information about the amount and timing of revenue that an entity expects to recognise from the remaining performance obligations in the entity's existing contracts. The boards observed that by disclosing that information, an entity would provide users of the entity's financial statements with additional information about the following:

- (a) the amount and expected timing of revenue to be recognised from the remaining performance obligations in existing contracts;
- (b) trends relating to the amount and expected timing of revenue to be recognised from the remaining performance obligations in existing contracts;
- (c) risks associated with expected future revenue (for example, some observe that revenue is more uncertain if an entity does not expect to satisfy a performance obligation until a much later date); and
- (d) the effect of changes in judgements or circumstances on an entity's revenue.

BC351 Many respondents (including most preparers) disagreed with the boards' decision to require such information to be disclosed in the financial statements. Those respondents highlighted different reasons for their disagreement, as follows:

- (a) the disclosure would be difficult and costly to prepare and audit because existing accounting systems are not designed to track and capture the required information, including the information on scheduling the timing of the satisfaction of those remaining performance obligations.
- (b) the information provided by the disclosure could be misinterpreted because, depending on the nature of the entity's business(es), the disclosure may give prominence to only a relatively small subset of the entity's potential future revenues. In addition, the disclosure may include less information than the entity previously included in its backlog disclosure because future and cancellable executory contracts are excluded from the scope of the disclosure.
- (c) the information appeared to be forward-looking in nature and thus should not be presented in the notes to the financial statements.

BC352 In redeliberating the disclosure requirements, taking into consideration the feedback received at the disclosure workshops, the boards observed that the requirement to disclose information about remaining performance obligations should not impose significant incremental costs on an entity because the entity is already required by the revenue recognition requirements to determine and allocate the transaction price to the remaining performance obligations. Nonetheless, the boards decided to address preparers' concerns about costs of preparation as follows:

- (a) providing practical expedients to limit the scope of the disclosure (see paragraph 121 of IFRS 15). The boards decided that including the practical expedient in paragraph 121(a) of IFRS 15 would ease the burden for the preparation of the disclosure and yet would not significantly decrease the usefulness of the information for users of financial statements. This is because users indicated that information for remaining performance obligations is most critical to their analyses when the contracts are long-term. In addition, including the practical expedient in paragraph 121(b) of IFRS 15 would maintain the relief provided to an entity in paragraph B16 of IFRS 15 on measuring progress for those performance obligations (ie performance obligations for which the entity has a right to consideration that corresponds directly with its performance completed to date). The boards provided practical expedients rather than specifically limiting the scope because some preparers commented that it would be easier for them to comply with the requirement from an accounting systems and processes perspective if they could choose to include all of their remaining performance obligations in the disclosure.
- (b) eliminating the prescriptive approach to disclosing when the entity expects to satisfy its remaining performance obligations (see paragraph 120 of IFRS 15). Initially, the boards proposed that an entity should follow a prescriptive approach in determining when the entity expects to satisfy its remaining performance obligations (ie by requiring a quantitative disclosure of the remaining performance obligations, scheduled into one-year time bands). However, many respondents disagreed with that proposal on the basis that the rigid nature of the prescribed time bands would imply a degree of precision in the timing of revenue recognition that may not exist and, furthermore, would increase the costs of preparation. In response to that feedback, the boards decided to permit an entity to estimate and present such information either on a quantitative basis, with time bands that are most appropriate for the duration of the remaining performance obligations (ie not necessarily one-year time bands) or by using qualitative information (or both).

BC353 Some users of financial statements also asked for more information to be provided about the relationship between the amounts disclosed as an entity's remaining performance obligations and the entity's contract liabilities. (A contract liability arises if an entity receives consideration from a customer before the entity satisfies its performance obligations to the customer.) This is because the amount of the remaining performance obligations for which cash has been received is useful information. However, the boards noted that contract liabilities are a subset of the amounts disclosed as the transaction price allocated to the remaining performance obligations and paragraph 116(a) of IFRS 15 already requires the contract liability balance to be disclosed. Consequently, the boards decided that no further disclosures should be required.

Performance obligations (paragraph 119)

- BC354 Previous requirements in IFRS and US GAAP require entities to disclose their accounting policies for recognising revenue (see paragraph 10(e) of IAS 1 and the requirements in Topic 235 *Notes to Financial Statements*). However, users of financial statements suggested that in many cases, an entity provides a 'boilerplate' description of the accounting policy adopted without explaining how the accounting policy relates to the contracts that the entity enters into with customers. To address this criticism, paragraph 119 of IFRS 15 requires that an entity disclose information about its performance obligations in contracts with customers. This disclosure complements the accounting policy disclosure requirements in existing Standards by requiring an entity to provide more descriptive information about its performance obligations.

Significant judgements (paragraphs 123–126)

- BC355 IFRS and US GAAP have general requirements for disclosing significant accounting estimates and judgements made by an entity. Because of the importance placed on revenue by users of financial statements, the boards decided to require specific disclosures about the estimates used and the judgements made in determining the amount and timing of revenue recognition.

Assets recognised from the costs to obtain or fulfil a contract with a customer (paragraphs 127–128)

- BC356 The boards decided to require that an entity disclose information about assets that it recognises from the costs to obtain or fulfil a contract, because information about those assets is useful to users. That information will help users of financial statements understand the types of costs that the entity has recognised as assets and how those assets are subsequently amortised or impaired. The boards also decided that this disclosure was necessary to replace some of the previous disclosure requirements that were superseded by IFRS 15.
- BC357 The boards decided not to require that information to be provided as a reconciliation because the cost of providing such a rigid disclosure would outweigh the benefit to users. In addition, most users agreed that the disclosure about the assets recognised from the costs to obtain or fulfil a contract did not need to be provided as a reconciliation to provide relevant information. Consequently, the boards decided to require disclosure of only the most critical information about assets recognised from the costs to obtain or fulfil a contract.

Disclosures required for interim financial reports

- BC358 The boards observed that in the absence of more specific disclosure requirements for interim financial reports, an entity should apply IAS 34 *Interim Financial Reporting* or Topic 270 *Interim Reporting* to determine the information about revenue from contracts with customers that the entity should disclose in its interim financial reports. Those requirements require, as

a general principle, an entity to disclose information about significant changes in its financial position and performance since the end of the last annual reporting period. The boards considered whether to amend IAS 34 and Topic 270 to specify that the entity provide the same quantitative disclosures about revenue in its interim financial reports as those in its annual financial statements.

- BC359 Many preparers and other respondents broadly disagreed with the boards' proposals to make amendments to IAS 34 and Topic 270. They explained that requiring all of the quantitative disclosures in interim financial reports would be too burdensome and difficult to achieve in the short time frames required for interim reporting. In contrast, users of financial statements had mixed views. Some users (including nearly all US-based users) suggested that IAS 34 and Topic 270 should be amended to require the quantitative disclosures because of the importance of revenue and the need to have timely disclosures provided regularly in the interim financial reports. However, other users of financial statements explained that only the information about the disaggregation of revenue was critical to their interim analyses. Those users of financial statements also explained that timeliness in interim reporting was critical and that a requirement to provide other interim disclosures might unnecessarily delay the issuance of interim financial reports.
- BC360 The IASB and the FASB reached different decisions on the amendments to IAS 34 and Topic 270. The IASB decided to amend IAS 34 to only add specific requirements that an entity should disclose disaggregated revenue information in interim financial reports. For all other disclosures related to revenue from contracts with customers, the IASB decided that the general principles of IAS 34 should apply. The IASB decided to add to IAS 34 a requirement to disclose disaggregated revenue information because users of financial statements explained that disaggregation was critical to their analyses and because the information is typically already provided in interim financial statements; therefore, the requirement should not result in an entity incurring significant incremental costs. Furthermore, the general principle of IAS 34 to disclose information about an entity's significant changes in financial position and performance should provide users of financial statements with the other information they need about revenue at an interim reporting period. The IASB decided not to make further changes to IAS 34 without a more comprehensive review of the role of disclosure in interim financial reporting.
- BC361 The FASB decided to amend Topic 270 to require the same quantitative disclosures about revenue in its interim financial reports as those in its annual financial statements (excluding the cost disclosures). The FASB noted that it is helpful to provide entities with certainty about the information that should be provided in interim financial reports. In addition, the FASB observed that an entity would be compiling most of the information required for the disclosures on an interim basis for the purposes of revenue recognition, and therefore disclosing that information might not result in a significant amount of incremental costs. The FASB also observed that this information is useful to

users of financial statements in assessing an entity's current and future financial performance.

Application guidance (paragraphs B2–B89)

BC362 The boards decided to include application guidance to clarify how the principles in IFRS 15 should be applied, including how those principles should be applied to features found in a number of typical contracts with customers. Some of that application guidance has been included based on previous requirements in IFRS or US GAAP that arose as a result of entities requesting clarification in more complex areas of revenue recognition. However, to be consistent with the objective of developing a single revenue recognition model, the boards did not provide requirements that would have applied only to specific industries (see paragraphs BC2–BC3).

Sale with a right of return (paragraphs B20–B27)

BC363 In some contracts, an entity transfers a good to a customer and also grants the customer the right to return it. The boards decided that, conceptually, a contract with a right of return includes at least two performance obligations – a performance obligation to provide the good to the customer and a performance obligation for the return right service, which is a stand-ready obligation to accept the goods returned by the customer during the return period.

BC364 In relation to performance obligations to provide customers with goods, the boards decided that, in effect, an entity has made an uncertain number of sales. This is because it is only after the return right expires that the entity will know with certainty how many sales it has made (ie how many sales did not fail). Consequently, the boards decided that an entity should not recognise revenue for the sales that are expected to fail as a result of customers exercising their return rights. Instead, the entity should recognise a liability for its obligation to refund amounts to customers.

BC365 The boards decided that in determining the amount of revenue to recognise (ie the amount of the refund obligation), an entity should use the principles for recognising and measuring variable consideration. Using those principles, an entity would recognise revenue only to the extent that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur when the uncertainty associated with the right of return is subsequently resolved. When the entity determines that it cannot recognise all of the consideration received as revenue for the sale of goods with a right of return, the entity would recognise some of the consideration received as a refund liability.

BC366 The boards considered whether to account for the return right service as a performance obligation, in addition to any refund liability that is recognised. If an entity does not recognise a performance obligation for the return right service, it should recognise all of the revenue and margin in the contract once the customer obtains control of the good. That outcome might not faithfully depict the entity's performance under the contract. However, the boards

noted that accounting for the return right service as a performance obligation, in addition to the refund liability, would typically require the entity to estimate the stand-alone selling price of that service. Because, in many cases, the number of returns is expected to be only a small percentage of the total sales and the return period is often short (such as 30 days), the boards decided that the incremental information provided to users of financial statements by accounting for the return right service as a performance obligation would not have justified the complexities and costs of doing so. Consequently, the boards decided that the return right service should not be accounted for as a performance obligation.

- BC367 A return right gives an entity a contractual right to recover the good from a customer if the customer exercises its option to return the good and obtain a refund. The boards decided that the right to recover the good should be recognised as an asset rather than offset against the refund liability. The boards observed that recognising the asset separately from the refund liability provides greater transparency and ensures that the asset is considered for impairment testing.

Warranties (paragraphs B28–B33)

- BC368 When an entity sells a product (whether that product is a good or service) to a customer, the entity may also provide the customer with a warranty on that product. The warranty might be described as, for example, a manufacturer's warranty, a standard warranty or an extended warranty. The boards decided to provide specific requirements for applying the revenue recognition model to warranties, because many contracts with customers for the sale of products include a warranty and the nature of that warranty may vary across products, entities and jurisdictions.
- BC369 In the Discussion Paper, the boards proposed accounting for all warranties consistently because a unifying feature of all warranties is that an entity promises to stand ready to replace or repair the product in accordance with the terms and conditions of the warranty. The Discussion Paper proposed that a promise to stand ready would provide a customer with a service of warranty coverage, which would have been a performance obligation to which revenue would be attributed. However, most respondents to the Discussion Paper stated that the accounting for warranties should reflect the fact that some product warranties are different from others. Some warranties protect the customer from defects that exist when the product is transferred to the customer and other warranties protect the customer from faults that arise after the product has been transferred to the customer. Those respondents commented that the customer does not receive a separate service if the warranty only protects the customer from the product defects that were present at the time of sale. Consequently, any subsequent repairs or replacements to remedy those defects are additional costs of providing the product and, therefore, relate to an entity's past performance.

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BC370 In the light of that feedback, the boards decided to account for some warranties differently from others. The boards considered distinguishing warranties on the basis of when the fault in the products arises; however, respondents explained that such a distinction was not operational. Therefore, the boards decided to distinguish warranties on the basis of whether the warranty provides the customer with a service in addition to the assurance that the related product complies with the agreed-upon specifications. Specifically, the boards decided that when the warranty provides a service (ie a service-type warranty), the warranty should be accounted for as a performance obligation.

Warranties that are performance obligations (service-type warranties)

BC371 For some types of warranties, an entity either sells separately or negotiates separately with a customer so that the customer can choose whether to purchase the warranty coverage. That fact provides objective evidence that the promised warranty provides a service to the customer in addition to the promised product. Consequently, the boards decided that this type of promised warranty is a performance obligation in accordance with paragraphs 22–30 of IFRS 15.

BC372 The boards decided that warranties that are not sold separately by the entity, or negotiated separately with the customer, should also be identified as performance obligations if the facts and circumstances suggest that the warranty (or a part of the warranty) provides a service to the customer, in addition to the assurance that the entity's past performance was as specified in the contract. The boards noted the following about this decision:

- (a) it provides a clear principle that allows an entity to account for economically similar warranties in a similar manner, regardless of whether the warranties are separately priced or negotiated;
- (b) it is consistent with the general principles for identifying performance obligations; and
- (c) it removes the bright line in previous US GAAP that distinguishes between different types of warranties based solely on whether the warranty is separately priced.

BC373 A warranty that meets the requirements in paragraphs B28–B33 of IFRS 15 to be accounted for as a performance obligation might also meet the criteria for classification as an insurance contract. However, only warranties issued directly by a third party would be accounted for as insurance contracts according to the proposals in the boards' respective projects on the accounting for insurance contracts.

Warranties that are not performance obligations (assurance-type warranties)

BC374 The boards considered whether an assurance-type warranty should be accounted for as either of the following:

- (a) a separate liability to replace or repair a defective product; or

- (b) an unsatisfied performance obligation, because the entity has not provided the customer with a product that is free from defects at the time of sale.

BC375 The proposals in the 2010 Exposure Draft would have required an entity that provides an assurance-type warranty to a customer to assess whether it had satisfied its performance obligation to transfer the product specified in the contract. The entity would have been required to determine the likelihood of the existence of defective products that it had sold to customers and their quantity and, as a consequence, not recognise revenue to the extent that those performance obligations were not satisfied. An advantage of that proposal would have been that an entity would not have recognised the entire transaction price as revenue when the product transferred to the customer, because a portion of the transaction price would not have been recognised as revenue until the entity had repaired or replaced the products that were expected to be defective. However, the boards decided not to retain that proposal, mainly for the following practical reasons:

- (a) there would have been complexities associated with the requirements for an entity to continue to recognise as 'inventory' products that had been delivered to customers and that were expected to be defective; and
- (b) any margin attributable to the repair or replacement of a product in an assurance-type warranty would have been unlikely to significantly distort the pattern of recognition of the overall contract margin.

BC376 Accordingly, the boards decided that an entity should recognise an assurance-type warranty as a separate liability to replace or repair a defective product. Consequently, an entity should recognise a warranty liability and corresponding expense when it transfers the product to the customer and the liability should be measured in accordance with IAS 37 or Topic 460 *Guarantees*. In contrast to the accounting for service-type warranties, an entity should not attribute any of the transaction price (and therefore revenue) to an assurance-type warranty. Some warranties may include both assurance features and service features. The boards decided that if an entity cannot reasonably account for those assurance features of the warranty separately from the service features, the entity should be allowed to account for the warranties together as a single performance obligation. That accounting ensures that the entity does not overstate the recognition of revenue at the time that the product transfers to the customer and also relieves the entity from identifying and accounting separately for the two components of the warranty coverage.

Statutory warranties

BC377 In some jurisdictions, the law requires an entity to provide warranties with the sale of its products. The law might state that an entity is required to repair or replace products that develop faults within a specified period from the time of sale. Consequently, those statutory warranties may appear to be service-type warranties because they cover faults arising after the time of sale, not merely defects existing at the time of sale. However, the boards decided that

the law can be viewed as simply operationalising an assurance-type warranty. In other words, the objective of those statutory warranties is to protect the customer against the risk of purchasing a defective product. But rather than requiring the entity to determine whether the product was defective at the time of sale, the law presumes that if a fault arises within a specified period (which can vary depending on the nature of the product), the product was defective at the time of sale. Consequently, these statutory warranties should be accounted for as assurance-type warranties.

Product liability laws

BC378 The boards clarified that product liability laws do not give rise to performance obligations. Those laws typically require an entity to pay compensation if one of its products causes harm or damage. The boards noted that an entity should not recognise a performance obligation arising from those laws because the performance obligation in a contract is to transfer the product to the customer. To the extent that an entity expects the product(s) to be defective, the entity should recognise a liability for the expected costs to repair or replace the product (see paragraph B33 of IFRS 15). Any obligation of the entity to pay compensation for the damage or harm that its product causes is separate from the performance obligation. The boards noted that an entity should account for this obligation separately from the contract with the customer and in accordance with the requirements for loss contingencies in IAS 37 or Topic 450.

Principal versus agent considerations (paragraphs B34–B38)⁶

BC379 Previous revenue Standards required an entity to assess whether it was acting as a principal or an agent when goods or services were transferred to a customer. That assessment was necessary to determine whether an entity should recognise revenue for the gross amount of customer consideration (if the entity was determined to be a principal) or for a net amount after the supplier was compensated for its goods or services (if the entity was determined to be an agent).

BC380 IFRS 15 also requires an entity to determine whether it is a principal or an agent. This is because the performance obligations of principals and agents are different. A principal controls the goods or services before they are transferred to a customer. Consequently, the principal's performance obligation is to transfer those goods or services to the customer. Therefore, recognising revenue at the gross amount of the customer consideration faithfully depicts the consideration to which the entity is entitled for the transfer of the goods

⁶ *Clarifications to IFRS 15* issued in April 2016 amended the application guidance in paragraphs B34–B38 and, as a consequence, amended paragraph BC383. The objective of amending the application guidance in paragraphs B34–B38 is to (a) provide a better framework to be applied when assessing whether an entity is a principal or an agent; (b) clarify the application of the control principle to intangible goods and services; and (c) clarify the role of the indicators in paragraph B37 when applying the control principle. Paragraphs BC379–BC385 should therefore be read together with paragraphs BC385A–BC385Z, which explain the boards' considerations for amending the application guidance.

and services. In contrast, an agent does not control the goods or services before they are transferred to a customer. The agent merely facilitates the sale of goods or services between a principal and the customer. Consequently, an agent's performance obligation is to arrange for another party to provide the goods or services to the customer. Therefore, the transaction price attributable to an agent's performance obligation is the fee or commission that the agent receives for providing those services.

- BC381 The boards observed that identifying an entity's promise (ie the performance obligation) in a contract is fundamental to the determination of whether the entity is acting as a principal or an agent. This is because identifying the nature of the entity's performance obligation is necessary for the entity to determine whether it controls the goods or services that have been promised before they are transferred to a customer. For example, a travel agent could be the principal in some contracts with customers if the travel agent determines that its promise is to provide a right to a flight (ie a ticket), instead of a promise to provide the flight. However, to conclude whether they are a principal or an agent, the travel agent would need to also consider whether it controlled that right before transferring it to the customer, which may occur when the travel agent purchases the tickets in advance for sales to future customers.
- BC382 The nature of the entity's promise may not always be readily apparent. For that reason, the boards included indicators in paragraph B37 of IFRS 15 to help an entity determine whether the entity controls the goods or services before transferring them and thus whether the entity is a principal or an agent. Those indicators are based on indicators that were included in previous revenue recognition requirements in IFRS and US GAAP. However, as noted in paragraph BC380, the indicators in IFRS 15 have a different purpose than previous revenue recognition requirements in that they are based on the concepts of identifying performance obligations and the transfer of control of goods or services.
- BC383 After an entity identifies its promise and determines whether it is the principal or the agent, the entity would recognise revenue when it satisfies its performance obligation. This would, for an entity that is a principal, occur when control of the promised goods or services transfers to the customer. The boards observed that in some contracts in which the entity is the agent, control of the goods or services promised to the customer might transfer before the customer receives the goods or services from the principal. For example, an entity that issues loyalty points to its customers when they purchase goods or services from the entity might satisfy its performance obligation with respect to the loyalty points on issuing those points to the customers if:
- (a) the points entitle the customers to future discounted purchases with another party (ie the points represent a material right to a future discount); and

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- (b) the entity determines that it is an agent (ie its promise is to arrange for the customers to be provided with points) and the entity does not control those points before they are transferred to the customer.

BC384 In contrast, the boards observed that if the points entitle the customers to future goods or services to be provided by the entity, the entity may conclude it is not an agent. This is because the entity's promise is to provide those future goods or services and thus the entity controls both the points and the future goods or services before they are transferred to the customer. In these cases, the entity's performance obligation may only be satisfied when the future goods or services are provided.

BC385 In other cases, the points may entitle customers to choose between future goods or services provided by either the entity or another party. The boards observed that in those cases, to determine when the performance obligation is satisfied, the entity would need to consider the nature of its performance obligation. This is because until the customer has chosen the goods or services to be provided (and thus whether the entity or the third party will provide those goods or services), the entity is obliged to stand ready to deliver goods or services. Thus, the entity may not satisfy its performance obligation until such time as it either delivers the goods or services or is no longer obliged to stand ready. The boards also observed that if the customer subsequently chooses the goods or services from another party, the entity would need to consider whether it was acting as an agent and thus should recognise revenue for only a fee or commission that the entity received from providing the services to the customer and the third party. The boards noted that this is consistent with previous revenue recognition requirements in IFRS for customer loyalty programmes.

Clarifications to IFRS 15 (amendments issued in April 2016)

BC385A The TRG discussed a number of issues in relation to paragraphs B34–B38 of IFRS 15. Some stakeholders asked whether control is always the basis for determining whether an entity is a principal or an agent, and how the control principle and the indicators in paragraph B37 work together. Other stakeholders asked how to apply the control principle to contracts involving intangible goods or services. In the light of those discussions and the feedback received, the boards discussed, and decided to clarify, the principal versus agent guidance by making the same targeted amendments to the application guidance and the related Illustrative Examples in IFRS 15 and Topic 606.

BC385B When another party is involved in providing goods or services to a customer, the amendments to the application guidance clarify how an entity determines whether it is a principal or an agent. These amendments focus on (a) the need for appropriately identifying the good or service that is transferred to the customer (the 'specified good or service'); and (b) determining whether the entity has promised to provide the specified good or service itself (ie the entity is a principal) or to arrange for the specified good or service to be provided to the customer by the other party (ie the entity is an agent). The entity determines the nature of its promise on the basis of whether the entity controls the specified good or service before that good or service is transferred

to the customer. Throughout the guidance on principal versus agent considerations, the boards decided to refer to the *specified good or service* transferred to the customer (as in paragraph B34), rather than the *performance obligation*. This is because use of the term ‘performance obligation’ would have been confusing if the entity is an agent. An agent’s performance obligation is to arrange for the other party to provide its goods or services to the customer; it does not promise to provide the goods or services itself to the end customer. Accordingly, the specified good or service to be provided to the end customer is not the performance obligation of the agent.

Principle for determining whether an entity is a principal or an agent

- BC385C Paragraph B34 requires an entity to determine whether it is a principal or an agent on the basis of whether the nature of the entity’s promise is a performance obligation to provide the specified goods or services itself (ie the entity is a principal) or to arrange for those goods or services to be provided by another party (ie the entity is an agent). Assessing whether the entity controls the specified good or service before it is transferred to the customer is the basis for determining the nature of the entity’s promise.
- BC385D The boards observed that in order for an entity to conclude that it is providing the specified good or service to the customer, it must first control that good or service (as defined in paragraph 33). The entity cannot provide the specified good or service to a customer if the entity does not first control the good or service to be provided. If an entity controls the specified good or service before that good or service is transferred to the customer, the entity is the principal in the transaction with the customer. If the entity does not control the specified good or service before that good or service is transferred to a customer, the entity is not a principal in the transaction with the customer. The boards noted that their considerations in this respect are explained in paragraph BC380.
- BC385E In addition, the boards noted that an entity that itself manufactures a good or performs a service is always a principal if the entity transfers control of that good or service to another party. Such an entity does not need to evaluate whether it is a principal or an agent using the guidance in paragraphs B34–B38 because the entity transfers the good or provides the service directly to its customer, without the involvement of another party. If the entity transfers a good or provides a service to an intermediary that is a principal in providing that good or service to an end customer (whether individually or as part of a distinct bundle of goods or services), the entity’s customer is the intermediary.
- BC385F Because of the concerns highlighted in the TRG’s discussions, the boards decided to clarify the following aspects of the application guidance on principal versus agent considerations:
- (a) the relationship between the control principle and the indicators in paragraph B37; and
 - (b) the application of the control principle to intangible goods and services.

The relationship between control and the indicators in paragraph B37

- BC385G The boards observed that the questions about the relationship between the assessment of control and the indicators of control in paragraph B37 arose, at least in part, because the indicators in that paragraph were carried forward from IAS 18 *Revenue* and Topic 605 *Revenue Recognition*. IAS 18 had a principle for this assessment (based on risks and rewards) that was different from the control principle in IFRS 15 and, although Topic 605 did not explicitly include a principle, the indicators in Topic 605 were understood to be indicators of risks and rewards. In addition, the structure of the analysis in Examples 45–48 accompanying IFRS 15 added to the confusion.
- BC385H The boards' considerations (explained in paragraph BC382) highlight that the indicators in paragraph B37 were included to support an entity's assessment of whether it controls a specified good or service before transfer in scenarios for which that assessment might be difficult. The indicators (a) do not override the assessment of control; (b) should not be viewed in isolation; (c) do not constitute a separate or additional evaluation; and (d) should not be considered a checklist of criteria to be met, or factors to be considered, in all scenarios. Considering one or more of the indicators will often be helpful and, depending on the facts and circumstances, individual indicators will be more or less relevant or persuasive to the assessment of control.
- BC385I The boards acknowledged that the indicators are similar to those in IAS 18 and Topic 605, but also noted their considerations in this respect, explained in paragraph BC382. Paragraph BC382 explains that the boards decided to carry over some of the indicators in previous revenue recognition Standards even though those indicators have a different purpose in IFRS 15. In IFRS 15, the indicators support the concepts of identifying performance obligations and the transfer of control of goods or services. Accordingly, the boards had expected that the conclusions about principal versus agent under IFRS 15 could be different in some scenarios from those reached under the previous revenue recognition Standards. Furthermore, the boards observed that, although exposure to risks and rewards alone does not give an entity control, exposure to risks and rewards can be a helpful factor to consider in determining whether an entity has obtained control (see paragraph 38).
- BC385J The boards decided to amend the indicators in paragraph B37 to more clearly establish a link between the control principle and the indicators by:
- (a) reframing the indicators as indicators of when an entity controls a specified good or service before transfer, rather than as indicators that an entity does not control the specified good or service before transfer.
 - (b) adding guidance to explain how each indicator supports the assessment of control as defined in paragraph 33 of IFRS 15. This should help entities apply indicators that are similar to those in the previous revenue recognition Standards but within the context of the control principle in IFRS 15.

- (c) removing the indicator relating to the form of the consideration. Although that indicator might sometimes be helpful in assessing whether an entity is an agent, the boards concluded that it would not be helpful in assessing whether an entity is a principal.
- (d) removing the indicator relating to exposure to credit risk. The feedback on the Exposure Draft *Clarifications to IFRS 15* highlighted that exposure to credit risk is generally not a helpful indicator when assessing whether an entity controls the specified good or service. Stakeholders observed that the credit risk indicator in the previous revenue guidance has been problematic from the perspective of entities trying to use exposure to credit risk to override stronger evidence of agency. The boards concluded that removing the credit risk indicator should reduce some of the complexity in the principal versus agent evaluation because the credit risk indicator will typically be less relevant, or not relevant, to the evaluation for contracts within the scope of IFRS 15.
- (e) clarifying that the indicators are not an exhaustive list and merely support the assessment of control—they do not replace or override that assessment. The boards decided to explicitly state that one or more of the indicators might provide more persuasive evidence to support the assessment of control in different scenarios.

BC385K In the light of the IASB's decision to generally apply a high hurdle when considering whether to amend IFRS 15, the IASB initially thought that it would not be necessary to add explanatory text to each indicator in paragraph B37 to establish a link to the concept of control. In the IASB's view, clarity about the interaction between the control principle and the indicators could have been achieved by amending only the Illustrative Examples. The IASB noted concerns about adding explanatory text to the indicators in paragraph B37 because of (a) the risk of new questions arising with respect to those additional explanations; and (b) the risk that some of those additional explanations might be used inappropriately to reach a conclusion that an entity is a principal when the entity is an agent. Nonetheless, despite those concerns, the IASB decided to amend the indicators in paragraph B37 of IFRS 15 in order to align the wording of the amendments with the wording of those made by the FASB. The IASB concluded that the benefits of retaining converged requirements on this topic outweigh the potential costs of amending the requirements.

The use of the indicators in paragraph B37 rather than the indicators in paragraph 38

BC385L Some stakeholders asked why the indicators in paragraph B37 are different from the indicators on the satisfaction of performance obligations (paragraph 38), noting that both sets of indicators relate to control. The boards observed that the indicators in paragraph 38 are indicators of the point in time at which the customer obtains control of the promised good or service. Accordingly, the indicators in paragraph 38 serve a different purpose than the indicators in paragraph B37. The indicators in paragraph 38 are not intended

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to indicate whether the customer obtains control of a promised asset—within the context of IFRS 15 as a whole, it is assumed that the customer will obtain control of the promised asset at some point—instead, they are intended to indicate when the customer has obtained control. In contrast, the indicators in paragraph B37 are intended to indicate whether the entity controls a specified good or service before that good or service is transferred to the customer.

Application of the control principle to intangible goods and services

BC385M The boards observed that at least some of the difficulty that stakeholders had in applying the control principle, in particular to intangible goods and services, was linked to challenges in identifying the specified good or service to be provided to the customer. The boards observed that this also had frequently been a challenge for entities under previous revenue recognition Standards.

BC385N The principal versus agent considerations relate to the application of Step 2 of the revenue recognition model. Appropriately identifying the good or service to be provided is a critical step in appropriately identifying whether the nature of an entity's promise is to act as a principal or an agent. When the appropriate specified good or service is identified, the assessment of control is often relatively straightforward, even when the specified good or service is an intangible good or a service. For example, the specified good or service to be provided to the customer could be:

- (a) a right to goods or services (see paragraph 26). For example, the airline ticket (a right to fly) in Example 47 and the meal voucher (a right to a meal) in Example 48 accompanying IFRS 15; or
- (b) a bundle of goods or services that are not distinct from each other (for example, the specialised equipment in Example 46 accompanying IFRS 15).

BC385O The boards observed that when the specified good or service to be provided to the customer is a right to goods or services to be provided in the future by another party, the entity would determine whether its performance obligation is a promise to provide a right to goods or services or whether it is arranging for the other party to provide that right. The fact that the entity will not provide the goods or services itself is not determinative. Instead, the entity evaluates whether it controls the right to goods or services before that right is transferred to the customer. In doing so, it is often relevant to assess whether the right is created only when it is obtained by the customer, or whether the right to goods or services exists before the customer obtains the right. If the right does not exist before the customer obtains it, an entity would be unable to control that right before it is transferred to the customer.

BC385P Some respondents to the Exposure Draft stated that it could be difficult in some cases to determine whether the specified good or service is the right to a good or service to be provided by another party or the underlying good or service itself (for example, in the case of Example 47, whether the specified good or service is the right to the flight (the ticket) or the flight itself). The

boards observed that a careful consideration of the facts and circumstances, and exercise of judgement may be required in identifying the specified good or service (just as identifying an entity's performance obligations outside the context of a principal versus agent evaluation will often require judgement). The boards also observed that assessing whether an entity controls a right to a good or service to be provided by another party is important to the principal versus agent evaluation. The boards noted that the Illustrative Examples accompanying IFRS 15 on principal versus agent considerations have been designed to address and explain scenarios in which the specified good or service is a right to a good or service to be provided by another party (as in Example 47 accompanying IFRS 15) and scenarios in which the specified good or service is the underlying service itself (as in Example 46A accompanying IFRS 15).

- BC385Q The boards also observed that the specified good or service to which the control principle is applied should be a distinct good or service, or a distinct bundle of goods or services. If individual goods or services are not distinct from each other, then they may be, for example, merely inputs to a combined item and are each only part of a single promise to the customer. Accordingly, an entity should evaluate the nature of its promise (ie to act as a principal or an agent) within the context of the promise to the customer, rather than for part of that promise. Consequently, for contracts in which goods or services provided by another party are inputs to a combined item (or items) for which the customer has contracted, the entity assesses whether it controls the combined item before that item is transferred to the customer.
- BC385R When a specified good or service is a distinct bundle of goods or services, the principal versus agent analysis may, in some cases, be straightforward. The boards concluded (in paragraph B35A(c)) that when an entity provides a significant service of integrating two or more goods or services into the combined output that is the specified good or service for which the customer contracted, it controls that specified good or service before it is transferred to the customer. When the entity provides a significant integration service it controls the inputs to the combined item that is the specified good or service (including goods or services provided by another party that are inputs to the specified good or service). The entity controls the inputs by directing their use to create the combined item. In that case, the inputs provided by the other party would be a fulfilment cost to the entity. In contrast, if a third party provides the significant integration service, then the entity's customer for its goods or services (which would be inputs to the specified good or service) is likely to be the other party.
- BC385S Consequently, the boards decided to clarify the thought process to be applied when assessing whether an entity is a principal or an agent by specifically requiring an entity to identify the specified good or service before applying the control principle to each specified good or service. The amended paragraph B34 and the additional paragraph B34A should:
- (a) provide a better framework for assessing whether an entity is a principal or an agent.

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- (b) emphasise the importance of appropriately identifying the specified good or service (which could be a right to a good or service to be provided by another party) that will be transferred to the customer.
- (c) clarify that the specified good or service (ie the unit of account for the principal versus agent evaluation) is each distinct good or service (or distinct bundle of goods or services). Accordingly, those paragraphs also clarify that, because a contract with a customer could include more than one specified good or service, an entity could be a principal for one or more specified goods or services in a contract and an agent for others.
- (d) emphasise that control (as defined in paragraph 33 of IFRS 15) is the determining factor when assessing whether an entity is a principal or an agent.

BC385T The IASB noted that, in many respects, paragraph B34A simply points to other relevant parts of the requirements in IFRS 15. Accordingly, the IASB did not view the inclusion of that additional paragraph as essential to clarifying the requirements in IFRS 15. In its view, clarity about the thought process to be applied could have been achieved by amending only the Illustrative Examples. Nonetheless, given the concerns raised by stakeholders, the IASB concluded that including paragraph B34A would be helpful to the principal versus agent evaluation, and would align the wording of the amendments with the wording of those made by the FASB. Therefore, the IASB concluded that the benefits of adding the paragraph outweigh the potential costs of amending the requirements.

Assessment of control of a service

BC385U The TRG's discussions highlighted concerns about the application of the control principle to services to be provided to a customer. Questions discussed included how an entity (other than the service provider) could control a service before that service is transferred to the customer, because a service comes into existence only at the moment that it is delivered. The boards observed that an entity can control a service to be provided by another party when it controls the right to the specified service from the other party that will be provided to the customer. The entity then either transfers the right to the service to the customer (for example, the airline ticket in Example 47) or uses its right to direct the other party to provide the service to the customer on the entity's behalf (ie to satisfy the entity's performance obligation in the contract with the customer), such as in Example 46A. Determining whether the entity controls a right to a specified service requires consideration of the facts and circumstances. The boards noted that contracts involving services provided by another party in which the entity is a principal can be broadly categorised as follows:

- (a) Contracts in which an entity provides the customer with a right to a future service to be provided by another party, such as the right to a specified flight (in the form of a ticket) to be provided by an airline (as discussed in paragraph BC385O).

- (b) Contracts in which the service provided by the other party is not distinct from other goods or services promised to the customer, and the entity directs the use of that service to create the combined item that is the specified good or service for which the customer has contracted (as discussed in paragraphs BC385Q–BC385R). Paragraph B35A(c) states that this scenario would exist whenever the entity provides a significant service of integrating the service provided by another party into the specified good or service for which the customer has contracted. Example 46 accompanying IFRS 15 illustrates this scenario.
- (c) Contracts in which an entity directs another party to provide the service to the customer on the entity's behalf in satisfying the entity's performance obligation. Example 46A accompanying IFRS 15 illustrates this scenario.

BC385V The boards observed that determining whether an entity is a principal or an agent may be more difficult in the third category of contracts listed above in which the entity has entered into a contract with a customer and has engaged another party (a subcontractor) to satisfy a performance obligation within that contract on its behalf. In these contracts, the entity assesses whether it controls a right to the specified services. An entity could control the right to the specified services by entering into a contract with the subcontractor and defining the services to be performed by the subcontractor on the entity's behalf. In that scenario, which is illustrated in Example 46A, the entity obtains the right to the services of the subcontractor and then directs the subcontractor to provide the services to the customer on the entity's behalf. This scenario is equivalent to the entity fulfilling the contract using its own resources rather than engaging another party to do so. The entity would remain responsible for the satisfactory provision of services in accordance with the contract with the customer. In other scenarios in which the specified services provided to the customer are provided by another party and the entity did not have the ability to direct those services, the entity would typically be an agent. In those scenarios, the entity is likely to be facilitating (and arranging for) the provision of services by the other party rather than controlling the rights to the services that the entity then directs to the customer.

BC385W The boards noted that paragraph B35 explains that an entity that is a principal in a contract may satisfy a performance obligation by itself or it may engage another party to satisfy some or all of a performance obligation on its behalf. The boards decided to add further explanation (paragraph B35A) to clarify the assessment of control of a service by explaining the scenarios in which a principal can control a service to be provided by another party. The boards also decided to add Example 46A to the Illustrative Examples accompanying IFRS 15 to illustrate the application of control to services.

Estimating revenue as a principal

- BC385X Some TRG participants asked how an entity that is a principal would estimate the amount of revenue to recognise if it were not aware of the amounts being charged to end customers by an intermediary that is an agent. The IASB observed that this question is largely unrelated to the application guidance on principal versus agent considerations in paragraph B34–B38 of IFRS 15, but rather relates to applying the requirements in paragraphs 46–90 on determining the consideration to which an entity is entitled. The IASB noted that the situations in which an entity that is a principal may be unaware of the amount charged to end customers by an intermediary that is an agent are generally limited to situations in which the intermediary (a) has some flexibility in setting prices; or (b) is procuring the good or service on behalf of the end customer. The IASB concluded that the issue does not require any clarifications or additional guidance because the issue is expected to affect a limited number of entities and contracts.
- BC385Y The FASB has also decided not to amend Topic 606 to address this issue. This is mainly because the FASB had observed that the situations in which an entity that is a principal is (and expects to remain) unaware of the amount charged by an intermediary that is an agent to the end customer are not pervasive and the issue affects only a limited number of entities and contracts. For those limited situations, the FASB is of the view that the determination of whether revenue may be estimated is based on an assessment of the requirements for determining the transaction price and estimating variable consideration.
- BC385Z The IASB did not specifically consider how the transaction price requirements would be applied in those situations but concluded that an entity that is a principal would generally be expected to be able to apply judgement and determine the consideration to which it is entitled using all relevant facts and circumstances available to it.

**Customer options for additional goods or services
(paragraphs B39–B43)**

- BC386 In some contracts, customers are given an option to purchase additional goods or services. The boards considered when those options should be accounted for as a performance obligation. During those discussions, the boards observed that it can be difficult to distinguish between the following:
- (a) an option that the customer pays for (often implicitly) as part of an existing contract, which would be a performance obligation to which part of the transaction price is allocated; and
 - (b) a marketing or promotional offer that the customer did not pay for and, although made at the time of entering into a contract, is not part of the contract and that would not be a performance obligation in that contract.

- BC387 Similar difficulties in distinguishing between an option and an offer have arisen in US GAAP for the software industry. Previous US GAAP revenue recognition requirements for the software industry specified that an offer of a discount on future purchases of goods or services was presumed to be a separate option in the contract, if that discount was significant and also incremental both to the range of discounts reflected in the pricing of other elements in that contract and to the range of discounts typically given in comparable transactions. Those notions of 'significant' and 'incremental' form the basis for the principle of a material right that is used to differentiate between an option and a marketing or promotional offer. However, the boards observed that even if the offered discount is not incremental to other discounts in the contract, it nonetheless could, in some cases, give rise to a material right to the customer. Consequently, the boards decided not to carry forward that part of the previous revenue recognition requirements from US GAAP into IFRS 15.
- BC388 Some respondents asked the boards to clarify whether specific options, such as customer loyalty points, should be accounted for as a performance obligation when the arrangement involves more than two parties. This often occurs in a credit card arrangement in which an entity provides the credit card holder with points based on the amount of purchases made at other entities (often referred to as 'merchants'). The boards determined that the assessment of whether any loyalty points represent a performance obligation requires an analysis of the facts and circumstances in each arrangement. The boards decided not to provide any further guidance because the issue was specific to the credit card industry and the boards observed that these arrangements are often complex and can vary significantly. Furthermore, the boards noted that IFRS 15 includes all the requirements to enable entities to account for the various arrangements.

Allocating the transaction price

- BC389 In accordance with IFRS 15, an entity is required to determine the stand-alone selling price of the option so that it can allocate part of the transaction price to that performance obligation. In some cases, the stand-alone selling price of the option may be directly observable. In many cases though, the stand-alone selling price of the option will need to be estimated.
- BC390 Option pricing models can be used to estimate the stand-alone selling price of an option. The price of an option includes the intrinsic value of the option (ie the value of the option if it were exercised today) and its time value (ie the value of the option that depends on the time until the expiry and the volatility of the price of the underlying goods or services). The boards decided that the benefits to users of financial statements of allocating some of the transaction price to the price and availability guarantees inherent in the time value component of the option price would not have justified the costs and difficulties to do so. However, the boards decided that an entity should be able to readily obtain the inputs necessary to measure the intrinsic value of the option in accordance with paragraph B42 of IFRS 15 and that those calculations should be relatively straightforward and intuitive. This measurement approach is consistent with the application guidance that was

provided for measuring customer loyalty points in previous revenue recognition requirements in IFRS.

Renewal options

- BC391 A renewal option gives a customer the right to acquire additional goods or services of the same type as those supplied under an existing contract. This type of option could be described as a renewal option within a relatively short contract (for example, a one-year contract with an option to renew that contract for a further year at the end of the first and second years) or a cancellation option within a longer contract (for example, a three-year contract that allows the customer to discontinue the contract at the end of each year). A renewal option could be viewed similarly to other options to provide additional goods or services. In other words, the renewal option could be a performance obligation in the contract if it provides the customer with a material right that it otherwise could not obtain without entering into that contract.
- BC392 However, there are typically a series of options in cases in which a renewal option provides a customer with a material right. In other words, to exercise any option in the contract, the customer must have exercised all the previous options in the contract. The boards decided that determining the stand-alone selling price of a series of options would have been complex because doing so would have required an entity to identify various inputs, such as the stand-alone selling prices for the goods or services for each renewal period and the likelihood that the customers will renew for the subsequent period. In other words, the entity would have had to consider the entire potential term of the contract to determine the amount of the transaction price from the initial period that should be deferred until later periods.
- BC393 For that reason, the boards decided to provide an entity with a practical alternative to estimating the stand-alone selling price of the option. The practical alternative requires an entity to include the optional goods or services that it expects to provide (and corresponding expected customer consideration) in the initial measurement of the transaction price. In the boards' view, it is simpler for an entity to view a contract with renewal options as a contract for its expected term (ie including the expected renewal periods) rather than as a contract with a series of options.
- BC394 The boards developed two criteria to distinguish renewal options from other options to acquire additional goods or services. The first criterion specifies that the additional goods or services underlying the renewal options must be similar to those provided under the initial contract—that is, an entity continues to provide what it was already providing. Consequently, it is more intuitive to view the goods or services underlying such options as part of the initial contract. In contrast, customer loyalty points and many discount vouchers should be considered to be separate deliverables in the contract, because the underlying goods or services may be of a different nature.

BC395 The second criterion specifies that the additional goods or services in the subsequent contracts must be provided in accordance with the terms of the original contract. Consequently, the entity's position is restricted because it cannot change those terms and conditions and, in particular, it cannot change the pricing of the additional goods or services beyond the parameters specified in the original contract. That too is different from examples such as customer loyalty points and discount vouchers. For example, if an airline offers flights to customers in exchange for points from its frequent flyer programme, the airline is not restricted, because it can subsequently determine the number of points that are required to be redeemed for any particular flight. Similarly, when an entity grants discount vouchers, it has typically not restricted itself with respect to the price of the subsequent goods or services against which the discount vouchers will be redeemed.

Customers' unexercised rights (breakage) (paragraphs B44–B47)

BC396 Some respondents asked the boards to provide guidance on how to account for a customer's non-refundable prepayment for the right to receive goods or services in the future. Common examples include the purchase of gift cards and non-refundable tickets.

BC397 The boards noted that the requirements for the allocation of the transaction price to customer options implicitly explains how to account for situations in which the customer does not exercise all of its contractual rights to those goods or services (ie breakage). However, the boards decided to clarify how to account for breakage in situations in which there is only one performance obligation in the contract (ie how to account for breakage in customer options when there is no need to allocate the transaction price and, therefore, no need to determine a stand-alone selling price).

BC398 Consequently, the boards included application guidance on the accounting for breakage. Those requirements require the same pattern of revenue recognition as the requirements for customer options. Thus, an entity should recognise revenue from breakage as it performs under the contract on the basis of the transfer of the goods or services promised in the contract. This effectively increases the transaction price allocated to the individual goods or services transferred to the customer to include the revenue from the entity's estimate of unexercised rights. The boards decided that this approach represents the most appropriate pattern of revenue recognition for breakage, because if an entity expected that customers would exercise all of their rights (ie if the entity did not expect any breakage), it might increase the price of its goods or services. For example, an airline that sells non-refundable tickets would presumably charge a higher price per ticket if there was no expectation of breakage.

BC399 The boards also decided that an entity should recognise revenue for breakage only if it is highly probable that doing so would not result in a subsequent significant revenue reversal (see paragraphs 56–58 of IFRS 15). Otherwise, the entity's performance obligation to stand ready to provide future goods or services could be understated.

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- BC400 The boards considered but rejected an approach that would have required an entity to recognise estimated breakage as revenue immediately on the receipt of prepayment from a customer. The boards decided that because the entity has not performed under the contract, recognising revenue would not have been a faithful depiction of the entity's performance and could also have understated its obligation to stand ready to provide future goods or services.
- BC401 Some respondents questioned whether the accounting for breakage is consistent with that for customer options in IFRS 15. Those respondents explained that for customer options, breakage is taken into account when determining the stand-alone selling price of the option as required by paragraph B42 of IFRS 15. Therefore, those respondents were concerned that when the consideration is allocated between the option and another performance obligation, some of the breakage on the option would be recognised when the other performance obligation is satisfied, which could occur before any rights under the options are exercised by the customer. However, the boards observed that when there are two (or more) performance obligations, IFRS 15 requires an entity to allocate the overall consideration between the performance obligations based on their relative stand-alone selling prices and, therefore, any discount on the combined bundle of goods or services is allocated on that basis (unless the entity meets the requirements in paragraph 82 or 85 of IFRS 15 to allocate on another basis). In other words, any difference between the sum of the stand-alone selling prices of the option and the other promised goods or services compared with the overall consideration would be recognised when (or as) the entity transfers the goods or services promised in the contract, which is consistent with the pattern of revenue recognition for breakage when there is only one performance obligation.

Licensing (paragraphs B52–B63B)⁷

- BC402 In the 2011 Exposure Draft, the boards proposed that a licence grants a customer a right to use, but not own, intellectual property of the entity. Consequently, the 2011 Exposure Draft viewed the nature of the promised asset in a licence as a right to use an intangible asset that is transferred at a point in time. This is because the boards' view at that time was that there is a point at which the customer obtains the ability to direct the use of, and obtain substantially all of the benefits from, the right to use the intellectual property. However, the 2011 Exposure Draft also explained that revenue may be recognised over time for some contracts that include a licence if that licence is not distinct from other promises in the contract that may transfer to the customer over time.

⁷ *Clarifications to IFRS 15* issued in April 2016 deleted paragraph B57 and added paragraph B59A of IFRS 15 to clarify the application guidance on determining the nature of the entity's promise in granting a licence of intellectual property. Paragraphs BC402–BC414 should therefore be read together with paragraphs BC414A–BC414Y, which explain the IASB's considerations in amending the application guidance.

BC403 In the light of the feedback received on the 2011 Exposure Draft, the boards reconsidered whether the nature of the promised asset in a licence is always a right that transfers at a point in time. In the examples they considered, the boards observed that licences vary significantly and include a wide array of different features and economic characteristics, which lead to significant differences in the rights provided by a licence. In some of the examples, the boards observed that the customer might be viewed as not obtaining control of the licence at a point in time. This is because the intellectual property to which the customer has obtained rights is dynamic and will change as a result of the entity's continuing involvement in its intellectual property, including activities that affect that intellectual property. In those cases, the customer may not be able to direct the use of, and obtain substantially all of the remaining benefits from, the licence at the time of transfer. In other words, what the licence provides to the customer is access to the intellectual property in the form in which it exists at any given moment. (Those notions were supported by some respondents who opposed the proposal in the 2011 Exposure Draft that all distinct licences represent the transfer of a right to use an intangible asset.)

BC404 Consequently, the boards decided to specify criteria for determining whether the nature of the entity's promise in granting a licence is to provide a customer with a right to access the entity's intellectual property as it exists throughout the licence period, or a right to use the entity's intellectual property as it exists at a point in time when the licence is granted. The boards noted that these criteria were necessary to distinguish between the two types of licences, rather than strictly relying on the control requirements, because it is difficult to assess when the customer obtains control of assets in a licence without first identifying the nature of the entity's performance obligation.

BC405 However, the boards observed that before applying the criteria, an entity should assess the goods or services promised in the contract and identify, as performance obligations, the promises that transfer the goods or services to the customer.

Identifying the performance obligations

BC406 The boards observed that, as is the case with other contracts, contracts that include a licence require an assessment of the promises in the contract and the criteria for identifying performance obligations (see paragraphs 27–30 of IFRS 15). This would include an assessment of whether the customer can benefit from the licence on its own or together with other resources that are readily available (see paragraph 27(a) of IFRS 15) and whether the licence is separately identifiable from other goods or services in the contract (see paragraph 27(b) of IFRS 15). The boards observed that this assessment may sometimes be challenging because the customer can often obtain benefit from the licence on its own (ie the licence is capable of being distinct). However, in many cases, the customer can benefit from the licence only with another good or service that is also promised (explicitly or implicitly) in the contract; therefore, the licence is not separately identifiable from other goods or services in the contract. This may occur when:

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- (a) a licence forms a component of a tangible good and is integral to the good's functionality—software (ie a licence) is often included in tangible goods (for example, a car) and in most cases, significantly affects how that good functions. In those cases, the customer cannot benefit from the licence on its own (see paragraph 27(a) of IFRS 15) because the licence is integrated into the good (see paragraph 29(a) of IFRS 15); that is, the licence is an input to produce that good, which is an output.
- (b) a licence that the customer can benefit from only in conjunction with a related service—this may occur when an entity provides a service, such as in some hosting or storage services, that enables the customer to use a licence, such as software, only by accessing the entity's infrastructure. In those cases, the customer does not take control of the licence and, therefore, cannot benefit from (or use) the licence on its own (see paragraph 27(a) of IFRS 15) without the hosting service. In addition, the use of the licence is highly dependent on, or highly interrelated with, the hosting service (see paragraph 29(c) of IFRS 15).

BC407 If the customer cannot benefit from the licence on its own, and/or the licence cannot be separated from other promises in the contract, the licence would not be distinct and thus would be combined with those other promises (see paragraph 30 of IFRS 15). The entity would then determine when the single performance obligation is satisfied on the basis of when the good or service (ie the output) is transferred to the customer. The boards noted that in some cases the combined good or service transferred to the customer may have a licence as its primary or dominant component. When the output that is transferred is a licence or when the licence is distinct, the entity would apply the criteria in paragraph B58 of IFRS 15 to determine whether the promised licence provides the customer with access to the entity's intellectual property or a right to use the entity's intellectual property.

Developing the criteria for licences that provide a right to access

BC408 As noted in paragraph BC404, the boards decided to specify criteria in paragraph B58 of IFRS 15 for determining if the intellectual property will change and, thus, if a licence provides a customer with a right to access the entity's intellectual property. If those criteria are not met, the licence provides the customer with a right to use an entity's intellectual property as that intellectual property exists (in the form and with the functionality) at the point in time when the licence transfers to the customer. To ensure that all licences are accounted for as either a right of access or a right to use, the boards decided to specify criteria for only one type of licence. In determining for which type of licence they should develop criteria, the boards observed that it was easier to determine when the intellectual property to which the customer has rights was changing (ie was dynamic), rather than when it was static.

- BC409 In developing the criteria, the boards observed that the main factor that results in the intellectual property changing is when the contract requires, or the customer reasonably expects, that the entity undertakes activities that do not directly transfer goods or services to a customer (ie they do not meet the definition of a performance obligation). The activities may be part of an entity's ongoing and ordinary activities and customary business practices. However, the boards noted that it was not enough that the entity undertook activities, but also that those activities affected the intellectual property to which the customer has rights and, thus, exposes the customer to positive or negative effects. In those cases, the customer will essentially be using the most recent form of the intellectual property throughout the licence period. The boards observed that when the activities do not affect the customer, the entity is merely changing its own asset, which, although it may affect the entity's ability to provide future licences, would not affect the determination of what the licence provides or what the customer controls.
- BC410 The boards noted that the assessment of the criteria would not be affected by other promises in the contract to transfer goods or services (ie performance obligations) that are separate from the licence. This is because the nature and pattern of transfer of each (separate) performance obligation in a contract would not affect the timing of other promised goods or services in the contract and, thus, would not affect the identification of the rights provided by the licence. This is because, by definition, a performance obligation is separate from the other promises in the contract. Consider a contract to provide a car and ongoing maintenance services – that is, two distinct goods or services (and thus two separate performance obligations). In this case, it seems counterintuitive to include the promise to provide a (separate) maintenance service when determining the nature and timing of the entity's performance related to the transfer of the car. A similar example can be drawn from a contract that includes a software licence and a promise to provide a service of updating the customer's software (sometimes included in a contract as post-contract support), in which the post-contract support is identified as a distinct good or service. This is because the entity would not consider the post-contract support when determining when control of the software transfers to the customer. In other words, a promise to transfer separate updates to the licence would not be considered in the assessment of the criteria in paragraph B58 of IFRS 15 and, furthermore, would be specifically excluded by criterion (c) in that paragraph.
- BC411 The boards also noted that an entity would exclude the factors specified in paragraph B62 of IFRS 15 for the following reasons:
- (a) restrictions of time, geographical region or use that define the attributes of the asset conveyed in a licence—an entity would not consider restrictions of time, geographical region or use, because they define attributes of the rights transferred rather than the nature of the underlying intellectual property and the rights provided by the licence. Consider, for example, a term licence that permits the customer to show a movie in its theatre six times over the next two years. The restrictions in that example determine the nature of the asset that the

entity has obtained (ie six showings of the movie), rather than the nature of the underlying intellectual property (ie the underlying movie).

- (b) guarantees provided by the entity that it has a valid patent to intellectual property and that it will defend and maintain that patent – guarantees that the entity has a valid patent would not be included in the assessment of the criteria for determining the rights provided in a licence, because those promises are part of the entity's representation that the intellectual property is legal and valid (this notion was previously included in the 2011 Exposure Draft).

BC412 In developing the criteria, the boards considered, but rejected, differentiating licences based on the following factors:

- (a) term of the licence – the length of a licence term is a restriction that represents an attribute of the asset transferred and does not provide information on the nature of the underlying intellectual property or on the nature of the entity's promise. For those reasons, the licence term does not depict when a customer obtains control of the promised licence.
- (b) exclusivity – the 2010 Exposure Draft proposed to distinguish between licences (ie whether they were a performance obligation satisfied over time or at a point in time) on the basis of whether the licence was exclusive. Many respondents to the 2010 Exposure Draft explained that a distinction based on exclusivity was inconsistent with the control principle, because exclusivity does not affect the determination of the entity's performance. In addition, respondents stated that a distinction based on exclusivity would not be operational, because it would require the boards to provide more clarity on how the term 'exclusive' would be interpreted. The boards observed that exclusivity is another restriction that represents an attribute of the asset transferred, rather than the nature of the underlying intellectual property or the entity's promise in granting a licence.
- (c) consumption of the underlying intellectual property – the boards also considered but rejected an approach that would differentiate between licences on the basis of the amount of the underlying intellectual property that was used up, or consumed by, a licence. This is because the intellectual property can be divided in many ways such as by time, geographical region or other restriction on use, and the rights can be provided to more than one customer at the same time through different licences. Consequently, it would be difficult for an entity to determine how much of the intellectual property was consumed by a particular licence.
- (d) payment terms – the boards decided not to use payment terms to differentiate between licences. This is because payment terms are not indicative of whether the licence provides the customer with a right to access or right to use the intellectual property of the entity and thus when the performance obligation is satisfied. Instead, payment terms

will be agreed by the customer and the entity and will reflect other economic factors such as credit risk and potential cash flows of the asset.

- BC413 The boards also considered whether to include a criterion that differentiated the nature of an entity's promise when the promised consideration is dependent on the customer's sales from, or usage of, the licence (often referred to as a sales-based or a usage-based royalty). As a criterion for differentiating licences, this would have resulted in *all* of the promised consideration being recognised over time for such licences, including any fixed amount. The boards decided not to include royalties as a criterion for differentiating licences, because the existence of a sales-based or a usage-based royalty does not solely define performance over time. However, the boards observed that, in some cases, the existence of a sales-based or a usage-based royalty can indicate a 'shared economic interest' between the entity and the customer in the intellectual property being licensed and therefore the customer could reasonably expect that the entity will undertake activities that affect the intellectual property to which the licence relates. The boards also decided, however, to include an exception for the revenue recognition pattern of sales-based or usage-based royalties (see paragraphs BC415–BC421).

When is the performance obligation satisfied?

- BC414 The boards observed that when the licence provides the customer with a right to access the entity's intellectual property, the promised licence represents a performance obligation satisfied over time because the customer will simultaneously receive and benefit from the entity's performance as the performance occurs—that is, the criterion in paragraph 35(a) of IFRS 15 will be met. However, when the licence provides the customer with a right to use the entity's intellectual property, the boards decided that the performance obligation will be satisfied at a point in time. In those cases, an entity would need to assess the point in time at which the performance obligation is satisfied (ie when the customer obtains control of the licence) by applying paragraph 38 of IFRS 15. The boards also decided to specify that control of a licence could not transfer before the beginning of the period during which the customer can use and benefit from the licenced property. If the customer cannot use and benefit from the licenced property then, by definition, it does not control the licence. The boards noted that when viewed from the entity's perspective, performance may appear to be complete when a licence has been provided to the customer, even if the customer cannot yet use that licence. However, the boards observed that the definition of control in paragraph 33 of IFRS 15 focuses on the customer's perspective, as explained in paragraph BC121.

Clarifications to IFRS 15 (amendments issued in April 2016)

- BC414A The TRG discussed issues relating to the application of the licensing guidance in IFRS 15. The main issues discussed related to:
- (a) determining the nature of the entity's promise in granting a licence of intellectual property;

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- (b) the scope and applicability of the sales-based and usage-based royalties exception;
- (c) the effect of contractual restrictions in a licence on identifying the performance obligations in the contract; and
- (d) when the guidance on determining the nature of the entity's promise in granting a licence applies.

BC414B In the light of those discussions and the feedback received, the IASB decided to clarify the application guidance on licensing and the accompanying Illustrative Examples to improve its operability and understandability. In some cases, the IASB concluded that a clarification is not necessary because there is adequate guidance in IFRS 15 with sufficient explanation of the boards' considerations in the Basis for Conclusions. Except for the scope and applicability of the sales-based and usage-based royalties exception, the FASB reached different conclusions about whether and how to address stakeholder concerns.

Determining the nature of the entity's promise in granting a licence of intellectual property

BC414C IFRS 15 specifies criteria in paragraph B58 for determining whether the nature of the entity's promise in granting a licence is to provide a customer with a right to access the entity's intellectual property as it exists throughout the licence period, or a right to use the entity's intellectual property as it exists at a point in time when the licence is granted. In developing IFRS 15, the boards noted that these criteria were necessary because it is difficult to assess when the customer obtains control of assets in a licence without first identifying the nature of the entity's performance obligation.

BC414D Paragraph B57 of IFRS 15 (now deleted, see paragraph BC414J) explained that the determination of whether an entity's promise to grant a licence provides a customer with a right to access or a right to use an entity's intellectual property is based on whether the customer can direct the use of, and obtain substantially all of the remaining benefits from, a licence at the point in time at which the licence is granted. A customer can direct the use of, and obtain substantially all the benefits from, the intellectual property, if the intellectual property to which the customer has rights is not significantly affected by activities of the entity. In contrast, a customer cannot direct the use of, and obtain substantially all of the remaining benefits from, a licence at the point in time at which the licence is granted if the intellectual property to which the customer has rights changes throughout the licence period. The intellectual property will change when the entity continues to be involved with its intellectual property and undertakes activities that significantly affect the intellectual property to which the customer has rights. Paragraph B58 provides criteria to help an entity assess whether its activities 'change' the intellectual property to which the customer has rights, including whether the expected activities of the entity significantly affect the intellectual property to which the customer has rights.

- BC414E Stakeholders agree that activities that change the form or functionality of the intellectual property would represent activities that affect the intellectual property to which the customer has rights. However, stakeholders have indicated that it was unclear whether the reference in IFRS 15 to changes in the intellectual property solely refers to changes in the form or functionality of the intellectual property, or also includes changes in the value of the intellectual property. This had resulted in different interpretations about how to apply the criteria in paragraph B58(a). Some stakeholders held the view that, for activities to significantly affect the intellectual property to which the customer has rights, those activities must be expected to change the form or functionality of that intellectual property. They thought that changes that solely affect the value of the intellectual property do not significantly affect the intellectual property to which the customer has rights. Others thought that activities that significantly affect the value of the intellectual property are sufficient to conclude that the licence provides a right to access the intellectual property.
- BC414F The IASB decided to clarify the requirements of paragraph B58(a) by providing additional application guidance on when activities change the intellectual property to which the customer has rights in such a way that the ability of the customer to obtain benefit from the intellectual property is significantly affected. The IASB noted that the reference to form or functionality in paragraph B61 (and the Illustrative Examples and the Basis for Conclusions) was not intended to suggest that the nature of a licence is a right to access intellectual property only if the entity's activities significantly affect the form or functionality of the intellectual property to which the customer has rights. Determining the nature of a licence is defined by the criteria in paragraph B58, which do not refer to form or functionality.
- BC414G Paragraph B59A clarifies that the assessment of whether the entity's activities significantly change the intellectual property to which the customer has rights is based on whether those activities affect the intellectual property's ability to provide benefit to the customer. In some cases, the ability of the intellectual property to provide benefit to the customer is derived from the form or functionality of the intellectual property to which the customer has rights and, in other cases, from the value of that intellectual property. If the activities are expected to significantly change the form or functionality of the intellectual property, those activities are considered to significantly affect the customer's ability to obtain benefit from the intellectual property. If the activities do not significantly change the form or functionality, but the ability of the customer to obtain benefit from the intellectual property is substantially derived from, or dependent upon, the entity's activities after the licence is granted, then the activities are also considered to significantly affect the intellectual property (as long as those activities do not result in the transfer of a good or service to the customer). In these cases, it is not necessary for those activities to change the form or functionality of the intellectual property to significantly affect the ability of the customer to obtain benefit from the intellectual property. For example, in some circumstances (eg many licences of brands), the benefit of the intellectual

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property is derived from its value and the entity's activities to support or maintain that value.

- BC414H The IASB observed that intellectual property that has significant stand-alone functionality derives a substantial portion of its benefit from that functionality. Consequently, if the entity's activities do not significantly change the form or functionality of such intellectual property, then the entity's activities will not significantly affect the customer's ability to derive benefit from that intellectual property. Therefore, the IASB clarified that in these cases the criterion in paragraph B58(a) would not be met and the licence would be a right to use the intellectual property as it existed at the time that it was transferred.
- BC414I The IASB has not defined the term 'significant stand-alone functionality' but has made clarifications to the Illustrative Examples to illustrate when the intellectual property to which the customer has rights might have significant stand-alone functionality. In many cases, it will be clear when intellectual property has significant stand-alone functionality. If there is no significant stand-alone functionality, the benefit to the customer might be derived substantially from the value of the intellectual property and the entity's activities to support or maintain that value. The IASB noted, however, that an entity may need to apply judgement to determine whether the intellectual property to which the customer has rights has significant stand-alone functionality.
- BC414J The IASB has deleted paragraph B57. This is in response to stakeholder concerns that paragraph B57 has contributed to the confusion about whether the reference to change solely refers to changes in the form or functionality of intellectual property or also includes changes in the value of intellectual property. The IASB is of the view that the addition of paragraph B59A provides clarity about the intended meaning of change in intellectual property, which makes the discussion in paragraph B57 redundant within the context of the application guidance. The discussion in paragraph B57 explained the IASB's logic for the requirements for determining whether an entity's promise to grant a licence provides a customer with either a right to access or a right to use an entity's intellectual property. Accordingly, the IASB has incorporated the content of paragraph B57 into this Basis for Conclusions.
- BC414K Having considered the wider implications of amending IFRS 15 before its effective date, the IASB decided to clarify the approach to determining the nature of an entity's promise in providing a licence, rather than change that approach. The IASB is of the view that stakeholder concerns have been addressed adequately by providing greater clarity about how to apply the requirements within the Standard. The IASB acknowledge that, in some cases, the outcome of using its clarified approach may differ from the outcome achieved using the alternative approach contained in the amendments issued by the FASB (see paragraphs BC414L–BC414N).

Alternative approach developed by the FASB

- BC414L The FASB developed an alternative approach to determine whether a licence constitutes a right to access or a right to use, based on the nature of the intellectual property. The FASB explained that the basis for this approach is whether an entity's promise to a customer includes supporting or maintaining the intellectual property to which the customer has rights, which in turn largely depends on whether the intellectual property has significant stand-alone functionality.
- BC414M The FASB decided that intellectual property is either:
- (a) functional intellectual property, which is intellectual property that has significant stand-alone functionality and derives a substantial portion of its utility (ie its ability to provide benefit or value) from its significant stand-alone functionality. In this case, a customer generally obtains a licence for the right to use intellectual property unless the functionality of the intellectual property is expected to substantively change during the licence period as a result of activities of the entity that do not transfer a good or service to the customer and the customer is contractually or practically required to use the updated intellectual property; or
 - (b) symbolic intellectual property, which is intellectual property that does not have significant stand-alone functionality. Substantially all of the utility of symbolic intellectual property is derived from its association with the entity's past or ongoing activities, including its ordinary business activities. In this case, a customer obtains a licence for the right to access intellectual property.
- BC414N The FASB's approach looks to the nature of the intellectual property to determine whether the entity's activities significantly affect the intellectual property to which the customer has rights. The FASB's approach has the potential to result in some licences of symbolic intellectual property being classified as a right to access intellectual property, even though there is no expectation that the entity will undertake activities after making the intellectual property available to the customer. For example, the entity may own a brand that it does not support or maintain, but still grants licences to customers to use the brand in television or movie productions that are set in a time period during which the brand was active. Nonetheless, the FASB decided to adopt this alternative approach on the basis of feedback that the approach would be more operable than the approach contained in Topic 606 when it was issued in May 2014, particularly for entities with a significant number of licensing arrangements and those with diversified operations.

Contractual restrictions in a licence and the identification of performance obligations

- BC414O Some stakeholders suggested that it was unclear whether particular types of contractual restrictions would affect the identification of the promised goods or services in the contract. For example, an arrangement might grant a customer a licence of a well-known television programme or movie for a period of time (for example, three years), but the customer might be restricted

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to showing that licensed content only once per year during each of those three years. Those stakeholders acknowledged that paragraph B62 is clear that restrictions of time, geographical region or use do not affect the licensor's determination about whether the licence is satisfied over time or at a point in time. However, in their view, it was unclear whether contractual restrictions affect the entity's identification of its promises in the contract (ie whether the airing restrictions affect whether the entity has granted one licence or three licences). Subsequent to the publication, in July 2015, of the Exposure Draft *Clarifications to IFRS 15*, the TRG discussed some further examples considering whether particular contractual restrictions create separate promises or, instead, merely define attributes of a promise. The TRG also discussed time attributes within the context of applying paragraph B61 of IFRS 15 to renewals of, or extensions to, existing licences (see paragraphs BC414S–BC414U).

- BC414P Having considered the wider implications of amending IFRS 15 before its effective date, the IASB decided that no clarification on the identification of performance obligations in a contract containing one or more licences was necessary. This is because, in its view, the clarifications made to IFRS 15 by the amendments issued in April 2016 will assist all entities in applying the requirements for identifying performance obligations contained in paragraphs 22–30 of IFRS 15. Paragraphs BC405–BC406 of IFRS 15 explain that, as is the case with other contracts, contracts that include a promise to grant a licence to a customer require an assessment of the promises in the contract using the criteria for identifying performance obligations (see paragraphs 27–30 of IFRS 15). This assessment is done before applying the criteria to determine the nature of an entity's promise in granting a licence. Consequently, the entity considers all of the contractual terms to determine whether the promised rights result in the transfer to the customer of one or more licences. In making this determination, judgement is needed to distinguish contractual provisions that create promises to transfer rights to use the entity's intellectual property from contractual provisions that establish when, where and how those rights may be used.
- BC414Q The IASB considered Example 59 in the Illustrative Examples accompanying IFRS 15. The entity concludes that its only performance obligation is to grant the customer a right to use the music recording. When, where and how the right can be used is defined by the attributes of time (two years), geographical scope (Country A) and permitted use (in commercials). If, instead, the entity had granted the customer rights to use the recording for two different time periods in two geographical locations, for example, years X1–X3 in Country A and years X2–X4 in Country B, the entity would need to use the criteria for identifying performance obligations in paragraphs 27–30 of IFRS 15 to determine whether the contract included one licence covering both countries or separate licences for each country.
- BC414R The FASB decided to amend Topic 606 to confirm that the requirements about contractual restrictions of the nature described in paragraph B62 do not replace the requirement for the entity to identify the number of licences promised in the contract. Similarly to the IASB, the FASB also observed that judgement is often required in distinguishing a contract that contains a single

licence with multiple attributes from a contract that contains multiple licences to the customer that represent separate performance obligations.

Renewals of licences of intellectual property

BC414S As noted in paragraph BC414O, the TRG discussed the application of paragraph B61 of IFRS 15 within the context of licence renewals. Paragraph B61 states that ‘... revenue cannot be recognised for a licence that provides a right to use the entity’s intellectual property before the beginning of the period during which the customer is able to use and benefit from the licence’. Some stakeholders asked whether paragraph B61 applies to the renewal of an existing licence or whether the entity could recognise revenue for the renewal when the parties agree to the renewal.

BC414T The discussion at the TRG indicated that this is an area in which judgement is needed. This is because when the entity and the customer enter into a contract to renew (or extend the period of) an existing licence, the entity will evaluate whether the renewal or extension should be treated as a new licence or, alternatively, as a modification of the existing contract. A modification would be accounted for in accordance with the contract modifications requirements in paragraphs 18–21 of IFRS 15. The IASB noted that, although some diversity may arise, IFRS 15 provides a more extensive framework for applying judgement than its predecessor, IAS 18. Again, having considered the wider implications of amending IFRS 15 before its effective date, the IASB decided that a clarification about the application of the contract modification requirements specifically for renewals of licensing arrangements was not necessary.

BC414U The FASB decided to amend Topic 606 and provide an additional example to specify that the entity would generally not recognise revenue relating to the renewal until the beginning of the licence renewal period. Consequently, in some cases, this may result in the recognition of revenue with respect to the renewal or extension at a later date using Topic 606 than using IFRS 15.

When to consider the nature of the entity’s promise in granting a licence

BC414V Paragraph B55 requires an entity to apply the general revenue recognition model (paragraphs 31–38) to determine whether a performance obligation that contains a licence that is not distinct (in accordance with paragraph 27) is satisfied at a point in time or over time. Since IFRS 15 was issued, some stakeholders have asked when the licensing guidance on determining the nature of an entity’s promise applies to a performance obligation that contains a licence and other goods or services. Some held the view that paragraph B55 suggests that an entity would consider the nature of its promise in granting a licence only when the licence is distinct. Others noted that an entity would have to consider the nature of its promise in granting a licence, even when the licence is not distinct, to (a) determine whether a single performance obligation that includes a licence of intellectual property is satisfied over time or at a point in time; and (b) measure progress towards complete satisfaction of that single performance obligation if it is satisfied over time.

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- BC414W Again, having considered the wider implications of amending IFRS 15 before its effective date, the IASB decided that a clarification in this respect is not necessary. IFRS 15 and the explanatory material in the Basis for Conclusions provide adequate guidance to account for a licence that is combined with another good or service in a single performance obligation. An entity will, however, need to apply judgement to determine the nature of the performance obligation, and to select a method of measuring progress that is consistent with the objective of depicting the entity's performance.
- BC414X In making this judgement, the IASB noted that it did not intend for an entity to disregard the guidance on determining the nature of its promise in granting a licence when applying the general revenue recognition model. In some cases, it might be necessary for an entity to consider the nature of its promise in granting a licence even when the licence is not distinct. The IASB discussed an example in which an entity grants a 10-year licence that is not distinct from a one-year service arrangement. The IASB noted that a distinct licence that provides access to an entity's intellectual property over a 10-year period could not be considered completely satisfied before the end of the access period. The IASB observed that it would, therefore, be inappropriate to conclude that a single performance obligation that includes that licence is satisfied over the one-year period of the service arrangement. Paragraph BC407 further highlights that an entity considers the nature of its promise in granting the licence if the licence is the primary or dominant component (ie the predominant item) of a single performance obligation.
- BC414Y The FASB decided to make amendments that explicitly state that an entity considers the nature of its promise in granting a licence when applying the general revenue recognition model to a single performance obligation that includes a licence and other goods or services (ie when applying the requirements in Topic 606 equivalent to those set out in paragraphs 31–45 of IFRS 15). Consequently, when the licence is not the predominant item of a single performance obligation, this may result in an entity that applies Topic 606 considering the nature of its promise in granting a licence in a greater number of circumstances than an entity applying IFRS 15.

Consideration in the form of sales-based or usage-based royalties⁸

- BC415 The boards decided that for a licence of intellectual property for which the consideration is based on the customer's subsequent sales or usage, an entity should not recognise any revenue for the variable amounts until the uncertainty is resolved (ie when a customer's subsequent sales or usage occurs). The boards had proposed a similar requirement in the 2011 Exposure Draft because both users and preparers of financial statements indicated that it would not be useful for an entity to recognise a minimum amount of revenue for those contracts. This is because that approach would inevitably have required the entity to report, throughout the life of the contract,

⁸ *Clarifications to IFRS 15* issued in April 2016 added paragraphs B63A–B63B of IFRS 15 to clarify when an entity should recognise revenue for a sales-based or usage-based royalty using the requirement in paragraph B63 of IFRS 15. Paragraphs BC415–BC421 should therefore be read together with paragraphs BC421A–BC421J, which explain the boards' considerations in amending the application guidance.

significant adjustments to the amount of revenue recognised at inception of the contract as a result of changes in circumstances, even though those changes in circumstances are not related to the entity's performance. The boards observed that this would not result in relevant information, particularly in contracts in which the sales-based or usage-based royalty is paid over a long period of time.

- BC416 In redeliberating the 2011 Exposure Draft, the boards observed that because the restriction for a sales-based or usage-based royalty on a licence of intellectual property was structured to apply to only a particular type of transaction, other economically similar types of transactions might be accounted for differently. For example, the restriction would not apply to tangible goods that include a significant amount of intellectual property and, instead, any variable consideration to which the entity is entitled in exchange for those tangible goods would be considered under the general requirements for constraining estimates of variable consideration. Some respondents questioned the conceptual rationale for including a restriction that could in some cases result in an outcome that was not consistent with the requirement to recognise some or all of an estimate of variable consideration. Others asked whether they could apply the restriction by analogy if the promised good or service had characteristics similar to a licence of intellectual property and the consideration depended on the customer's future actions. Consequently, the boards considered whether they should do either of the following:
- (a) expand the scope of paragraph B63 of IFRS 15 to constrain all estimates of variable consideration when that consideration depends on the customer's future actions; or
 - (b) develop a general principle that could be applied to all contracts that would achieve broadly the same outcomes.

Expand the scope

- BC417 The boards considered whether to expand the restriction for a sales-based or usage-based royalty on a licence of intellectual property, whereby revenue recognition would be constrained to zero for any performance obligation when the amount that an entity is entitled to is based on a customer's future actions. However, the boards decided not to introduce this principle into IFRS 15. This is because it would have prevented an entity from recognising any revenue when the goods and services were transferred in cases in which the entity could estimate the variable consideration and meet the objective of constraining estimates of variable consideration.
- BC418 The boards also observed that expanding the scope to constrain revenue when consideration is based on the customer's future actions would also have increased complexity. It would have required the boards to create another exception to maintain the requirements for accounting for customer rights of return, which also results in consideration that is dependent on the customer's future actions.

Develop a general principle

- BC419 The boards also considered whether the restriction for a sales-based or usage-based royalty on a licence of intellectual property could be incorporated into a general principle. The boards considered various ways of articulating this principle, including doing so on the basis of the timing of satisfaction of a performance obligation—that is, whether the performance obligation is satisfied over time or at a point in time. Specifically, if the performance obligation to which the variable consideration related was satisfied at a point in time, an entity would include an estimate of variable consideration in the transaction price only to the extent that 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. Conversely, if the performance obligation to which the variable consideration related was satisfied over time, an entity could include any estimate in the transaction price (even a minimum amount) provided that the objective of constraining estimates of variable consideration could be met.
- BC420 This approach was based on the rationale that, for a performance obligation satisfied at a point in time, recognition of revenue that could be adjusted up or down would not be a meaningful depiction of the consideration for the related goods or services and, furthermore, any future adjustments to the transaction price (and therefore revenue) would have little correlation with the entity's performance in that period. Conversely, when a performance obligation is satisfied over time, the initial recognition of some but not all of the estimate of variable consideration would be affected by the entity's future performance, so future adjustments to the transaction price would provide useful information because they explain whether the entity's subsequent performance was beneficial (ie the minimum amount is increased) or detrimental (ie the minimum amount is subject to an unexpected reversal). However, the boards rejected this approach because it would have added complexity to the model that would outweigh the benefit.
- BC421 Consequently, the boards decided against applying the restriction for sales-based or usage-based royalties on intellectual property more broadly. Although the boards acknowledge that the requirements in paragraph B63 of IFRS 15 constitute an exception that might not be consistent with the principle of recognising some or all of the estimate of variable consideration, they decided that this disadvantage was outweighed by the simplicity of these requirements, as well as by the relevance of the resulting information for this type of transaction. The boards also noted that because this is a specific requirement intended for only limited circumstances, entities should not apply it by analogy to other types of promised goods or services or other types of variable consideration.

Clarifications to IFRS 15 (amendments issued in April 2016)

- BC421A Paragraph B63 requires an entity to recognise revenue for a sales-based or usage-based royalty promised in exchange for a licence of intellectual property when the later of the following events occurs: (a) the customer's subsequent sales or usage; and (b) the performance obligation to which some or all of the

sales-based or usage-based royalty has been allocated has been satisfied (or partially satisfied). This guidance in paragraph B63 is referred to as the 'royalties constraint'.

- BC421B Stakeholders had indicated that it was unclear when a sales-based or usage-based royalty is 'promised in exchange for a licence'. Some stakeholders held the view that the royalties constraint applies whenever the royalty relates to a licence of intellectual property, regardless of whether the royalty is also consideration for other goods or services in the contract. Other stakeholders had suggested that the royalties constraint applies only when the royalty relates solely to a licence that is distinct in accordance with paragraph 27 of IFRS 15 or only when the licence is the predominant item to which the royalty relates. Stakeholders had also indicated that it was unclear whether a single sales-based or usage-based royalty should be split into a portion to which the royalties constraint would apply and a portion to which it would not, for example, when the royalty relates to a licence and another good or service that is not a licence.
- BC421C In response to stakeholder concerns, the boards decided to clarify the application of the royalties constraint as follows:
- (a) the royalties constraint applies whenever a licence of intellectual property is the sole or predominant item to which the royalty relates; and
 - (b) an entity should not split a single royalty into a portion subject to the royalties constraint and a portion that is subject to the general constraint on variable consideration contained in paragraphs 50–59 of IFRS 15.

Applying the royalties constraint

- BC421D The boards decided to clarify in paragraph B63A that the royalties constraint applies to those arrangements for which the licence is the predominant item to which the royalty relates. This is because users of financial statements are likely to view those arrangements as licensing arrangements. The boards had previously observed in paragraph BC415 that it would not be useful for an entity to recognise a minimum amount of revenue for licences of intellectual property for which the consideration is based on the customer's sales or usage. Applying the royalties constraint only when the royalty relates solely to a licence that is distinct in accordance with paragraph 27 of IFRS 15 might unduly restrict its application.
- BC421E The boards observed that judgement is required to determine when a licence is the predominant item to which a sales-based or usage-based royalty relates. However, the judgement needed for that determination is likely to be less than the judgement needed to apply the general requirements on variable consideration to those arrangements that would fall outside the scope of the royalties constraint if that scope were to be more restrictive.

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- BC421F The boards decided against changing the scope of the royalties constraint, including expanding it beyond those situations for which a licence is the predominant item to which a royalty relates. This is because doing so would capture arrangements for which the boards previously concluded that the royalties constraint should not apply (for example, sales of intellectual property or sales of tangible goods that include intellectual property). As noted in paragraphs BC416 and BC421, the royalties constraint is intended to apply only to limited circumstances involving licences of intellectual property and, therefore, entities cannot apply it by analogy to other types of transactions.
- BC421G The boards observed that an entity might conclude that a licence is the predominant item to which a sales-based or usage-based royalty relates when there is more than one performance obligation. This conclusion might be reached regardless of whether the entity concludes that the royalty can be allocated entirely to one performance obligation in accordance with the requirements for allocating variable consideration in paragraphs 84–85 of IFRS 15. The boards also observed that the royalties constraint would also apply when the royalty predominantly relates to two or more licences promised in a contract, rather than a single licence.
- BC421H The boards made consistent clarifying amendments to the Illustrative Examples to more clearly support the conclusions reached about when a sales-based royalty would be recognised. However, the boards decided not to amend paragraph B63 or provide further Illustrative Examples for more complex fact patterns.
- BC421I In reaching this decision, the IASB considered a similar example to Example 60 accompanying IFRS 15 and concluded that when a time-based measure of progress appropriately depicts an entity's performance under the licence, recognising the sales-based royalty as and when the customer's sales occur would generally be appropriate. This is because, as noted in paragraph BC219, the objective of the royalties constraint is to prevent an entity from recognising revenue for uncertain amounts until the uncertainty is resolved (ie when the customer's subsequent sales or usage occurs). In effect, the requirement in paragraph B63 constrains the amount of revenue that can be recognised when or as a performance obligation is satisfied, rather than constraining the total amount of the transaction price to be allocated. Paragraph B63(b) reflects one of the key principles of IFRS 15, which is to recognise revenue only when (or as) an entity satisfies a performance obligation. If the entity has satisfied (or partially satisfied) the performance obligation to which the royalty relates, paragraph B63(a) further constrains the recognition of revenue until the uncertainty about the amount of revenue is resolved. Consequently, an entity recognises revenue from a sales-based or usage-based royalty when (or as) the customer's subsequent sales or usage occur, unless recognition in that manner would accelerate the recognition of revenue for the performance obligation to which the royalty solely or partially relates ahead of the entity's performance towards complete satisfaction of the performance obligation based on an appropriate measure of progress.

Splitting a royalty

- BC421J Paragraph B63B of IFRS 15 clarifies that an entity should recognise revenue from a sales-based or usage-based royalty wholly in accordance with either the requirement in paragraph B63 (if paragraph B63 applies) or the requirements on variable consideration contained in paragraphs 50–59 of IFRS 15 (if paragraph B63 does not apply). The boards made this clarification in paragraph B63B because the boards concluded that (a) it would be more complex to account for part of a royalty under the royalties constraint and another part under the general requirements for variable consideration; and (b) doing so would not provide any additional useful information to users of financial statements. This is because splitting a royalty would result in an entity recognising an amount at contract inception that would reflect neither the amount to which the entity expects to be entitled based on its performance, nor the amount to which the entity has become legally entitled during the period.

Repurchase agreements (paragraphs B64–B76)

- BC422 When developing the requirements for control, the boards considered how an entity should apply the requirements to contracts in which the entity sells an asset and also enters into a repurchase agreement (either in the same contract or in another contract).
- BC423 The boards observed that repurchase agreements generally come in three forms—forwards, call options and put options. However, the boards decided that an arrangement in which an entity subsequently decides to repurchase a good after transferring control of that good to a customer would not constitute a repurchase agreement as described in paragraph B64 of IFRS 15. This is because the entity's subsequent decision to repurchase a good without reference to any pre-existing contractual right does not affect the customer's ability to direct the use of, and obtain substantially all of the remaining benefits from, the good upon initial transfer. In other words, the customer is not obliged to resell that good to the entity as a result of the initial contract. The boards observed that in those cases, the entity should, however, consider whether the customer obtained control of the good initially and may need to consider the requirements for principal versus agent in paragraphs B34–B38 of IFRS 15.

A forward or a call option

- BC424 If an entity has an obligation or a right to repurchase an asset (ie a forward or a call option, respectively), the boards decided that the customer does not obtain control of the asset and, therefore, no revenue should be recognised. This is because the customer is constrained in its ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. Because the customer is obliged to return, or to stand ready to return, the asset to the entity, the customer cannot use up or consume the entire asset. Moreover, the customer cannot sell the asset to another party (unless that sale is subject to a repurchase agreement, in which case the customer's benefit from the sale is constrained).

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- BC425 Theoretically, a customer is not constrained in its ability to direct the use of, and obtain substantially all the benefits from, the asset if an entity agrees to repurchase, at the prevailing market price, an asset from the customer that is substantially the same and is readily available in the marketplace. However, the boards noted that an entity would be unlikely to enter into such a transaction.
- BC426 The boards decided that an entity would account for a forward or a call option as a lease or a financing arrangement, depending on the relationship between the repurchase amount and the original selling price. The FASB also decided to specify that when the forward or call option accounted for as a lease is part of a sale-leaseback transaction, the contract should be accounted for as a financing transaction. Otherwise, the FASB observed that an entity would have been required to account for the transaction as a lease and then as a leaseback, which would not have been appropriate.
- BC427 The boards noted that an entity would not need to consider the likelihood that a call option can be exercised, because the existence of the call option effectively limits the customer's ability to control the asset. However, the boards observed that if the call option is non-substantive, that option should be ignored in assessing whether and when the customer obtains control of a good or service (to be consistent with the general requirement for any non-substantive term in a contract).

A put option

- BC428 The boards decided that if the sale and repurchase agreement resulted in an entity's obligation to repurchase the asset at a customer's request (ie a put option), the customer would obtain control of the asset because the customer is neither obliged to return the asset nor obliged to stand ready to do so. Consequently, the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset (ie the customer can sell, use up or consume the entire asset and choose not to exercise the put option). The boards decided that the entity should account for its obligation to stand ready to repurchase the asset, to be consistent with the accounting for the sale of a product with a right of return (see paragraphs BC363–BC367). That results in the entity recognising the following:
- (a) a liability for its obligation to repurchase the asset, measured at the amount of the consideration expected to be paid to the customer;
 - (b) an asset for the entity's right to receive that asset upon settling that liability, measured at an amount that may or may not equal the entity's previous carrying value of the asset; and
 - (c) revenue on transfer of the asset for the difference between the sales price of the asset and the liability recognised for the obligation to repurchase the asset.
- BC429 Some respondents questioned whether that accounting would be appropriate in all cases in which a customer has a put option. For instance, some noted that the contract appears to be economically similar to a lease with a purchase option rather than to a right of return. That might be the case if the entity is

required to repurchase the asset at a price that is lower than the original sales price and the surrounding facts and circumstances indicate that the customer will exercise its put option. In those cases, the difference between the original sales price and the repurchase price can be viewed as the amount that the customer pays for a right to use the asset, thereby compensating the entity for the decline in the value of the asset. Some respondents noted that, in other cases, the contract is, in effect, a financing arrangement.

BC430 The boards agreed with those respondents and decided that if a customer has a right to require an entity to repurchase the asset at a price that is lower than the original sales price and the customer has a significant economic incentive to exercise that right, then the customer does not obtain control of the asset. Although the customer is not obliged to exercise its put option, the fact that it has a significant economic incentive to exercise that right means that it would probably incur a loss if it did not do so. (For example, the repurchase price may be set significantly above the expected market value of the asset at the date of the repurchase. However, the boards observed that an entity should consider factors other than the price when determining that it has a significant economic incentive to exercise its right.) The boards decided that in those cases, the existence of the option effectively restricts the customer's ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. For similar reasons, the boards decided that if the customer has the unconditional right to require the entity to repurchase the asset at a price that is greater than the original sales price, and higher than the expected market value of the asset, the customer does not obtain control of the asset.

BC431 The boards also considered whether other arrangements should be accounted for as a lease, such as when an entity provides its customer with a guaranteed amount to be paid on resale (ie a guaranteed minimum resale value). Accounting for those transactions as leases would be consistent with previous US GAAP, and a number of respondents, primarily from the automotive industry, explained that they viewed the transactions to be economically similar. However, the boards observed that while the cash flows may be similar, the customer's ability to control the asset in each case is different. If the customer has a put option that it has significant economic incentive to exercise, the customer is restricted in its ability to consume, modify or sell the asset. However, when the entity guarantees that the customer will receive a minimum amount of sales proceeds, the customer is not constrained in its ability to direct the use of, and obtain substantially all of the benefits from, the asset. Thus, the boards decided that it was not necessary to expand the requirements for repurchase agreements to consider guaranteed amounts of resale.

Accounting for repurchase agreements in which the customer does not obtain control of the asset

BC432 If an entity enters into a contract with a repurchase agreement and the customer does not obtain control of the asset, the boards decided the following:

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- (a) the contract should be accounted for as a lease in accordance with IAS 17 *Leases* or Topic 840 *Leases* if the customer is paying for a right to use the asset; and
- (b) the contract is a financing arrangement if the net consideration that the entity receives is equal to or less than zero (ie the entity is paying interest).

BC433 To ensure consistent accounting in IFRS and US GAAP for a financing arrangement that arises from a contract with a customer, the boards decided to provide guidance consistent with Subtopic 470-40 *Debt—Product Financing Arrangements*. Consequently, the FASB decided to amend the guidance in Subtopic 470-40 that discusses arrangements in which an entity sells a product to another entity and, in a related transaction, agrees to repurchase the product. However, the FASB decided not to amend Subtopic 470-40 for transactions in which an entity arranges for another party to purchase products on its behalf and agrees to purchase those products from the other party. In those cases, the entity is required to recognise the products as an asset and to recognise a related liability when the other party purchases the product. The FASB noted that although IFRS 15 results in similar accounting when the other party acts as an agent of the entity (ie the other party does not obtain control of the products), Subtopic 470-40 provides explicit requirements for transactions in which no sale has occurred.

Transition, effective date and early application (paragraphs C1–C9)

Transition (paragraphs C2–C8A)

BC434 The boards decided that an entity should apply IFRS 15 using either of the following methods:

- (a) retrospectively to each prior reporting period presented in accordance with IAS 8 or Topic 250 *Accounting Changes and Error Corrections*, subject to some optional practical expedients (see paragraphs BC435–BC438); or
- (b) retrospectively with the cumulative effect of initially applying IFRS 15 recognised as an adjustment to the opening balance of retained earnings at the date of initial application (see paragraphs BC439–BC444).

Retrospective application

BC435 The 2010 and 2011 Exposure Drafts proposed that an entity should apply the requirements retrospectively in accordance with IAS 8 or Topic 250. Retrospective application ensures that all contracts with customers are recognised and measured consistently both in the current period and in the comparative periods presented, regardless of whether those contracts were entered into before or after the requirements became effective. Furthermore, retrospective application provides users of financial statements with useful trend information across the current period and comparative periods.

Feedback received from users of financial statements confirmed that retrospective application would be the most useful transition approach for them to be able to understand trends in revenue.

BC436 In contrast to the feedback received from users of financial statements, many respondents commented that applying the requirements retrospectively would be burdensome, especially for entities with long-term contracts or large and complex multiple-element arrangements. The main concerns raised by those respondents were as follows:

- (a) it may not be possible to obtain historical information for contracts that were completed under previous revenue Standards in IFRS or US GAAP because the relevant information is no longer retained by the entity.
- (b) applying IFRS 15 retrospectively (particularly to completed contracts) may not result in a materially different pattern of revenue recognition, and the significant costs incurred to confirm this fact would not provide much benefit to users of financial statements. For example, for contracts that were considered to be completed (as assessed under previous revenue Standards) several years before the date of initial application, an entity would, theoretically, need to obtain the relevant information to ensure that there was no effect on the pattern of revenue recognition in the financial statements in the year of initial application.
- (c) presenting the effect of IFRS 15 in the comparative years would incur significant preparation and audit costs, because a change in revenue could affect many other line items in the financial statements (such as deferred tax, receivables, interest and foreign currency gains/losses) as well as items that reference an entity's revenue in the financial statements (such as taxes, statutory reporting and financing arrangements).
- (d) the historical information needed to estimate stand-alone selling prices of goods or services in a contract with many performance obligations may not exist.
- (e) entities make assumptions and estimates throughout a contract's life, and it may not be possible to recreate the circumstances that apply historically without the use of hindsight.

**Retrospective application with practical expedients
(paragraphs C4–C6)**

BC437 The boards decided that although retrospective application would generally impose increased preparation costs, those costs would be outweighed by the increased benefits to users of financial statements. Consequently, the boards considered how the burden of retrospective application could be eased while, at the same time, retaining the benefits of comparability and consistency that retrospective application would provide. To ease the burden of transition without sacrificing comparability, the boards decided to allow an entity to

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elect to use one or more of the following practical expedients when applying IFRS 15 retrospectively.

Practical expedient	Rationale
<i>Reducing the number of contracts that require restatement^(a)</i>	
<p>For contracts completed before the date of initial application of IFRS 15, an entity need not restate contracts that begin and end within the same annual reporting period.</p>	<p>In considering whether an entity should be required to review and restate all contracts completed before the date of initial application, the boards decided that trend information should be preserved for completed contracts that span annual reporting periods. Consequently, the boards decided to limit the relief to only those contracts that begin and end within the same annual reporting period, because the amount and timing of revenue recognition relating to those contracts would not change between annual reporting periods. The boards noted that this relief would significantly reduce the transition burden on entities that have a large number of short-term contracts.</p> <p>A consequence of this relief is that revenue reported in interim periods before and after the effective date would not necessarily be accounted for on a comparable basis. The boards expect that an entity would not elect to use this relief if it operates in an industry in which comparability across interim reporting periods is particularly important to users of financial statements.</p>
<i>Simplifying how an entity restates contracts with customers^(b)</i>	
<p>For contracts completed before the date of initial application of IFRS 15 and that have variable consideration, an entity may use the transaction price at the date that the contract was completed rather than estimating variable consideration amounts in the comparative reporting periods.</p>	<p>Full retrospective application of IFRS 15 in accordance with IAS 8 or Topic 250 would require an entity to determine the estimates that it would have made at each of the reporting dates in the comparative periods. The boards considered that making those estimates in the comparative years would increase the complexity and costs of retrospective application.</p> <p>By allowing an entity to use hindsight in estimating variable consideration, the boards decided that transition would be simplified for the following reasons:</p> <ul style="list-style-type: none"> (a) it would reduce the amount of information that an entity would need to collect throughout the transition period; and (b) the entity would not need to determine the transaction price at the end of each period.

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Practical expedient	Rationale
<i>Simplifying retrospective application of other aspects of the requirements</i>	
<p>For all reporting periods presented before the date of initial application of IFRS 15, an entity need not disclose the amount of the transaction price allocated to the remaining performance obligations and an explanation of when the entity expects to recognise that amount as revenue (as specified in paragraph 120 of IFRS 15).</p>	<p>The boards decided that the disclosure of the amount of the transaction price allocated to the remaining performance obligations (as would be required by paragraph 120 of IFRS 15) should not be required for periods presented before the date of initial application of IFRS 15 for the following reasons:</p> <p>(a) the disclosure would be most useful for the current period; and</p> <p>(b) the disclosure could be burdensome to prepare for comparative years, especially when trying to avoid the use of hindsight to estimate the transaction price and the expected timing of satisfaction of those performance obligations.</p>
<p>(a) <i>Clarifications to IFRS 15</i> issued in April 2016 amended paragraph C5 of IFRS 15 to add a further practical expedient to permit an entity not to restate contracts that are completed contracts at the beginning of the earliest period presented. This practical expedient, if applied, would further reduce the number of contracts that require restatement. The IASB's considerations in adding the practical expedient are explained in paragraphs BC445M–BC445N.</p> <p>(b) <i>Clarifications to IFRS 15</i> issued in April 2016 amended paragraph C5 and added paragraph C7A to add a further practical expedient to simplify how an entity restates contracts with customers that are modified before transition to IFRS 15. The boards' considerations in adding the practical expedient are explained in paragraphs BC445O–BC445R.</p>	

BC438 As a result of the practical expedients providing some relief from applying IFRS 15 retrospectively, the boards also decided to supplement the transitional disclosure requirements of IAS 8 or Topic 250 to require an entity to provide additional disclosure if it elects to use one or more of the practical expedients. Accordingly, paragraph C6 of IFRS 15 requires an entity to provide an explanation to users of financial statements about which practical expedients were used and, to the extent reasonably possible, a qualitative assessment of the estimated effect of applying those practical expedients.

Retrospective application with the cumulative effect recognised in the current period (paragraphs C7–C8)

BC439 The boards decided to develop an alternative transition method to ease the burden of retrospectively applying IFRS 15 because feedback from preparers and auditors indicated that, although helpful, the practical expedients (see paragraph BC437) would not mitigate much of the implementation challenge of a retrospective transition approach. In contrast, users of financial

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statements generally supported the requirements for retrospective application with practical expedients because it would provide them with useful information on transition and assist their financial statement analyses.

- BC440 As a result of those differing views, transition was one of the topics discussed at four disclosure and transition workshops that were held in late 2012 with both users and preparers of financial statements (see paragraph BC328). During those workshops, users of financial statements acknowledged that another transition method might be appropriate to ease the burden of transition; however, they emphasised their need for trend information, regardless of which method is used.
- BC441 After considering this feedback, the boards decided that as an alternative to retrospective application with practical expedients, an entity could apply IFRS 15 (including the requirements for costs) retrospectively, with the cumulative effect of initially applying IFRS 15 recognised in the current year (referred to as the ‘cumulative catch-up’ transition method). Specifically, the cumulative effect would be an adjustment to the appropriate opening balance of equity in the year of initial application (ie comparative years would not be restated) for contracts that are not completed at the date of initial application.⁹ (The boards clarified that a completed contract is a contract in which the entity has fully performed in accordance with revenue recognition requirements in effect before the date of initial application. Thus, a completed contract would include a contract for which the entity’s performance was complete but there was a change in the transaction price after the date of initial application.)¹⁰ The boards observed that the cumulative catch-up transition method responds to feedback from auditors and preparers by eliminating the need to restate prior periods and thus reducing costs.
- BC442 The boards noted that applying the cumulative catch-up transition method results in consistent presentation of contracts under previous IFRS or US GAAP during the comparative years and in consistent presentation of any contracts not yet completed at the date of initial application under IFRS 15 in the current year. However, because the comparative information will not be restated under the cumulative catch-up transition method, the boards decided to require additional disclosures to help users of financial statements understand the effect on trend information. Consequently, when an entity uses the cumulative catch-up transition method, it is required to disclose the following information for reporting periods that include the date of initial application:

⁹ *Clarifications to IFRS 15* issued in April 2016 amended paragraph C7 of IFRS 15 to permit an entity using the transition method described in paragraph C3(b) to apply IFRS 15 (a) only to contracts that are not completed contracts at the date of initial application (as originally required in paragraph C7 when IFRS 15 was issued); or (b) to all contracts including completed contracts at the date of initial application. The boards’ considerations in amending paragraph C7 are explained in paragraphs BC445J–BC445L.

¹⁰ The FASB subsequently decided to amend the definition of a completed contract as a contract for which all or substantially all of the revenue was recognised in accordance with the revenue guidance that was in effect before the date of initial application of Topic 606. The IASB’s considerations for deciding not to amend the definition, together with an overview of the FASB’s considerations for amending the definition, are explained in paragraphs BC445C–BC445I.

- (a) the amount by which each financial statement line item is affected in the current year as a result of the entity applying IFRS 15 rather than previous revenue Standards in IFRS; and
- (b) an explanation of the reasons for the significant changes in those financial statement line items.

BC443 In other words, to provide the required disclosures, an entity would apply both IFRS 15 and the previous revenue Standards in the year of initial application. Despite requiring an entity to account for revenue transactions in the year of initial application using two different sets of accounting requirements, the boards decided that this method would reduce the overall cost of applying IFRS 15 while still providing information about trends that was requested by users of financial statements.

BC444 The boards also considered other transition methods as alternatives to the cumulative catch-up method to try to ease the burden of retrospective application. For example, the boards considered requiring a prospective approach that would require entities to apply IFRS 15 only to new contracts or those that are materially modified on or after the date of initial application. However, the boards rejected this approach because prospective application would not result in consistent presentation of existing contracts and new contracts and thus would reduce comparability. In addition, this approach would not provide useful trend information for users of financial statements until existing contracts have been fully satisfied after the date of initial application. Furthermore, the boards observed that this approach would require some entities to incur significant costs of maintaining two accounting systems for contracts that are accounted for in accordance with IFRS 15 and previous revenue Standards in IFRS, until all existing contracts have been completed, which could take many years for entities with long-term contracts.

Other relief

BC445 If an entity applies IFRS 15 retrospectively in accordance with paragraph C3(a) of IFRS 15 (ie without electing to use the cumulative catch-up transition method), comparative information *would* be restated. Consequently, the IASB clarified that if an entity applies IFRS 15 retrospectively in accordance with paragraph C3(a), it is not required to provide the current year transition disclosure in paragraph 28(f) of IAS 8.

Clarifications to IFRS 15 (amendments issued in April 2016)

BC445A The boards discussed requests from some stakeholders for further transition relief in respect of (a) accounting for a completed contract (as defined in paragraph C2(b)) on transition to IFRS 15; and (b) accounting for modifications to a contract that occurred before transition to IFRS 15. The IASB decided (a) to expand the application of the transition method described in paragraph C3(b) by allowing an entity a choice to apply IFRS 15 to all contracts including completed contracts; and (b) to provide transition relief for contract modifications. The FASB decided to make similar amendments to Topic 606. The IASB additionally decided to allow an entity using the transition method described in paragraph C3(a) not to restate completed contracts at the

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beginning of the earliest period presented. The following paragraphs explain the boards' considerations in providing the additional practical expedients.

Completed contracts

BC445B The boards considered the following questions about the transition requirements in IFRS 15 with respect to a completed contract:

- (a) definition of and accounting for a completed contract.
- (b) providing an entity applying paragraph C3(b) of IFRS 15 with the choice of applying IFRS 15 to all contracts including completed contracts at the date of initial application.
- (c) permitting an entity applying paragraph C3(a) of IFRS 15 not to restate completed contracts at the beginning of the earliest period presented.

Definition of and accounting for a completed contract

BC445C Some stakeholders, mainly in the US, highlighted potential difficulties with respect to the definition of a completed contract in paragraph C2(b) and the accounting for a completed contract once IFRS 15 becomes effective. They were unclear whether the boards intended that any previously unrecognised revenue from a completed contract that is not transitioned to IFRS 15 would continue to be accounted for in accordance with the previous revenue Standards. In addition, referring to the words 'transferred all of the goods or services' in the definition of a completed contract, they commented that:

- (a) *transfer* of goods or services is a notion that is introduced in IFRS 15 and does not exist in previous revenue Standards.
- (b) it is unclear how an entity would continue to account for a completed contract in accordance with the previous revenue Standards, which would be withdrawn once IFRS 15 becomes effective.
- (c) the boards' considerations explained in paragraph BC444 for rejecting a prospective transition method do not support the use of the previous revenue Standards once IFRS 15 becomes effective. As explained in paragraph BC444, one of the reasons for rejecting prospective transition methods was the 'significant costs of maintaining two accounting systems...until all existing contracts have been completed, which could take many years for entities with long-term contracts'.

BC445D The IASB concluded that it was not necessary to change the definition of a completed contract to address the issues raised. In relation to the words 'transferred all of the goods or services' in the definition of a completed contract, the IASB noted that it did not intend that an entity would apply the 'transfer of control' notion in IFRS 15 to goods or services identified in accordance with previous revenue Standards. The IASB noted that paragraph BC441 refers to performance in accordance with previous revenue Standards. Consequently, in many situations the term 'transferred' would mean 'delivered' within the context of contracts for the sale of goods and 'performed' within the context of contracts for rendering services and construction contracts. In some situations, the entity would use judgement

when determining whether it has transferred goods or services to the customer. For example, an entity may need to use judgement to determine when it has transferred rights to use its assets (for example, rights granted within a licence agreement), because there is no specific guidance on the transfer or delivery of such rights in IAS 18.

- BC445E The IASB observed that if an entity chooses not to apply IFRS 15 to completed contracts in accordance with paragraph C5(a)(ii) or the amended paragraph C7, only contracts that are not completed contracts are included in the transition to IFRS 15. The entity would continue to account for the completed contracts in accordance with its accounting policies based on the previous revenue Standards. The IASB's decision, when it issued IFRS 15 in May 2014, was not to require such an entity to apply IFRS 15 either prospectively or retrospectively to completed contracts.
- BC445F Furthermore, the IASB also observed that its rationale for rejecting a prospective transition method because of the costs of maintaining two systems is less relevant to completed contracts for two reasons. First, the IASB expects the volume of completed contracts with unrecognised revenue at the date of transition to IFRS 15 to be significantly less than the volume of all ongoing contracts that would be included in the transition to IFRS 15. Second, for many completed contracts, the IASB does not expect the accounting under previous revenue Standards to continue for many years after transition, because the goods or services have been transferred before the transition to IFRS 15.
- BC445G Some stakeholders expressed a view that accounting for completed contracts using the previous revenue Standards after IFRS 15 becomes effective would not provide useful financial information to users of financial statements. When developing the transition method described in paragraph C3(b), the boards considered feedback from users of financial statements and decided to require an entity to provide additional disclosures to help users understand the effect of that transition method on trend information (see paragraphs BC442–BC443). The IASB observed that as part of the disclosures required by paragraph C8 an entity could provide additional information about the amount of revenue recognised using previous revenue Standards, if the entity concludes that such information would be helpful to users. In addition, when selecting a transition method, the IASB expects that an entity would consider whether the selected transition method provides useful information to users of its financial statements. If the entity were to conclude that excluding completed contracts from the transition to IFRS 15 would not provide useful information to users, and if that is an important consideration for the entity, then the entity could decide to include completed contracts in its transition to IFRS 15.
- BC445H The FASB decided to amend Topic 606 to define a completed contract as a contract for which all (or substantially all) of the revenue was recognised in accordance with the previous revenue Standards. The FASB believes that the objective of the transition guidance in Topic 606 should be to ensure that all (or substantially all) of the revenue from contracts with customers that is recognised after transition to Topic 606 should be recognised in accordance

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with Topic 606. Accordingly, the FASB decided to amend the definition of a completed contract so that an entity would apply Topic 606 to all contracts for which all (or substantially all) of the revenue was not recognised under the previous revenue Standards. The FASB acknowledged that an entity would need to apply judgement in some cases to determine whether a contract is completed.

BC445I The IASB observed that the boards' different decisions regarding amendments to the definition of a completed contract give rise to a difference between IFRS 15 and Topic 606. However, the IASB noted that an entity could avoid the consequences of the different definitions by choosing to apply IFRS 15 retrospectively to all contracts including completed contracts (see paragraph BC445K).

Providing an entity applying IFRS 15 in accordance with paragraph C3(b) with the choice of applying IFRS 15 to all contracts including completed contracts at the date of initial application

BC445J The boards decided to amend paragraph C7 to provide an entity with a choice of applying IFRS 15 in accordance with paragraph C3(b) either (a) only to contracts that are not completed contracts at the date of initial application (which was the original requirement in paragraph C7 when IFRS 15 was issued); or (b) to all contracts including completed contracts at the date of initial application. The boards acknowledged that this choice might result in a decrease in comparability between entities. However, the boards observed that applying the transition method described in paragraph C3(b) to all contracts, including completed contracts, at the date of initial application could result in financial information that is more comparable with financial information provided by entities using the transition method described in paragraph C3(a). Furthermore, the IASB observed that any decrease in comparability between entities because of the choice will be transitory.

BC445K The IASB also observed that:

- (a) an entity that wishes to use the transition method described in paragraph C3(b) and also avoid the consequences of the different definitions of a completed contract in IFRS 15 and Topic 606 could choose to apply IFRS 15 in accordance with paragraph C3(b) to all contracts including contracts that are completed contracts at the date of initial application; and
- (b) some entities will find applying the transition method described in paragraph C3(b) to all contracts less complex operationally than continuing to account for completed contracts under previous revenue Standards and all other contracts under IFRS 15, or using the method described in paragraph C3(a).

BC445L The FASB observed that allowing the choice may help mitigate some of the unanticipated financial reporting consequences that some entities may experience as a result of its amendments to the definition of a completed contract.

Permitting an entity applying IFRS 15 in accordance with paragraph C3(a) not to restate completed contracts at the beginning of the earliest period presented

- BC445M The IASB decided to provide an additional practical expedient to permit an entity applying IFRS 15 in accordance with paragraph C3(a) not to restate contracts that are completed contracts at the beginning of the earliest period presented. The IASB noted that reducing the population of contracts to which IFRS 15 applies (the consequence of applying this practical expedient) could reduce the effort and cost of initial application of IFRS 15. In addition, the IASB observed that a similar expedient is currently given to first-time adopters in paragraph D35 of IFRS 1 *First-time Adoption of International Financial Reporting Standards*.
- BC445N The FASB decided not to provide a similar expedient to the transition guidance because it concluded that application of such an expedient would not faithfully depict a full retrospective application of Topic 606. The IASB acknowledged that the expedient could affect the comparability of financial information under the full retrospective method, but concluded that this would be outweighed by the benefit provided by the reduced transition costs.

Modified contracts

- BC445O Some stakeholders highlighted that applying the requirements in paragraphs 20–21 of IFRS 15 to past contract modifications could be complex, especially if the entity has long-term contracts that are modified frequently. To simplify how an entity retrospectively applies IFRS 15 to its contracts with customers, the boards decided to provide an additional practical expedient that would permit an entity to use hindsight when evaluating contract modifications when making the transition to IFRS 15. Consequently, when restating contracts on transition to IFRS 15, an entity could either (a) follow the requirements in paragraphs 20–21; or (b) use the new practical expedient in paragraph C5(c) of IFRS 15. The new practical expedient allows the entity to reflect the aggregate effect of all past contract modifications when identifying the performance obligations, and determining and allocating the transaction price, instead of accounting for the effects of each contract modification separately. The boards observed that the practical expedient would provide some cost relief and yet would result in financial information that closely aligns with the financial information that would be available under IFRS 15 without the expedient.
- BC445P The boards' conclusions on the date at which this practical expedient should be applied are not fully aligned. Both boards decided that an entity applying IFRS 15 in accordance with paragraph C3(a) should apply the practical expedient at the beginning of the earliest period presented. For an entity applying Topic 606 in accordance with paragraph 606-10-65-1(d)(2) (equivalent to paragraph C3(b) of IFRS 15), the FASB decided that the entity should apply the practical expedient at the date of initial application. However, the IASB decided that an entity applying IFRS 15 in accordance with paragraph C3(b) may apply the practical expedient either (a) at the beginning of the earliest period presented; or (b) at the date of initial application.

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BC445Q The IASB observed that without the choice of the date at which the practical expedient is applied, entities that apply IFRS 15 in accordance with paragraph C3(b), especially entities with a large number of contracts subject to frequent modifications (for example, some telecommunication companies), might have practical difficulties if they are required to wait until the date of initial application for finalising the cumulative effect of past contract modifications. This is because of the large number of contracts that would have to be evaluated in a relatively short time. Those entities highlighted that the benefit of the practical expedient would be considerably constrained if they cannot finalise the cumulative effect of past contract modifications ahead of the date of initial application of IFRS 15. The IASB observed that this decision creates a difference between IFRS 15 and Topic 606. However, an entity applying IFRS 15 in accordance with paragraph C3(b) could avoid the different reporting outcomes between IFRS 15 and Topic 606 by choosing to apply the practical expedient at the date of initial application.

BC445R The boards considered, but rejected, permitting an entity to account for the unsatisfied performance obligations in a modified contract at transition as if the original contract were terminated and a new contract created as of the transition date. This would be computationally simpler because it eliminates the need to evaluate the effects of modifications before transition to IFRS 15. Under this approach, the amount of consideration allocated to the unsatisfied performance obligations would be the total consideration promised by the customer (including amounts already received) less any amounts already recognised as revenue under previous revenue Standards. Although this might significantly reduce the cost and complexity of applying the transition requirements to contract modifications, the approach was rejected by the boards because it could result in financial information that differed significantly from that under IFRS 15 without the expedient.

Transition to Clarifications to IFRS 15

BC445S The IASB decided to require an entity to apply the amendments to IFRS 15 retrospectively in accordance with IAS 8. In reaching its decision to require retrospective application, the IASB observed that the amendments were intended to clarify the IASB's intentions when developing the requirements in IFRS 15 rather than to change the underlying principles of IFRS 15. The IASB decided not to allow prospective application of the amendments because that would reduce comparability in the limited cases that the amendments may have resulted in significant changes to an entity's application of IFRS 15. This is consistent with feedback received from users of financial statements during the development of IFRS 15 highlighting that retrospective application would be the most useful transition method for them to understand trends in revenue.

BC445T By requiring an entity to apply the amendments as if those amendments had been included in IFRS 15 at the date of initial application, the IASB observed that:

- (a) if the entity applies both IFRS 15 and *Clarifications to IFRS 15* at the same time, any effect of applying the amendments would be reflected in the effects of initially applying IFRS 15.
- (b) if the entity applies *Clarifications to IFRS 15* after the date of initial application of IFRS 15, the effects of initially applying IFRS 15 would be restated for the effects, if any, of initially applying the amendments.

BC445U The outcome of retrospective application of *Clarifications to IFRS 15* will depend on which transition method an entity chooses when it first applies IFRS 15. The choice of the transition method will determine, for example, whether periods before the date of initial application of IFRS 15 are restated as well as the amount and date of the adjustment to retained earnings. Retrospective application of *Clarifications to IFRS 15* will affect only those reporting periods and those contracts to which IFRS 15 is applied. For example, consider an entity that applies IFRS 15 in accordance with paragraph C3(b) on 1 January 2017 and *Clarifications to IFRS 15* on 1 January 2018. Retrospective application of *Clarifications to IFRS 15* would not require the restatement of financial information before 1 January 2017 for the effects of the amendments. Any effect of applying the amendments would be included in a restated cumulative effect adjustment as of 1 January 2017.

Effective date and early application (paragraphs C1–C1B)

Effective date¹¹

BC446 In the 2011 Exposure Draft, the boards indicated that the effective date of IFRS 15 would be set to ensure that the start of the earliest comparative period for an entity that is required to present two comparative annual periods (in addition to the current annual period) would be after the final requirements are issued. The boards developed this approach in response to feedback obtained from interested parties through a number of activities, including:

- (a) the IASB's Request for Views on *Effective Dates and Transition Methods* and the FASB's Discussion Paper *Effective Dates and Transition Methods* (October 2010);
- (b) the boards' joint investor outreach questionnaire (April 2011); and
- (c) consultation with systems providers and preparers in 2010 and 2011.

BC447 On the basis of that proposed formula for setting an effective date and of the estimated issue date of IFRS 15 at the time of their decision, the boards would have set the effective date as 1 January 2016. However, many respondents, including respondents in industries for which there could be significant process and system changes required to comply with IFRS 15 (for example, in the telecommunications and software industries), indicated that the proposed formula would not provide them with adequate time. Specifically, those respondents explained that providing only a short time before the earliest comparative period would not be sufficient to ensure that processes and

¹¹ The boards subsequently deferred the effective date of IFRS 15 and Topic 606 by one year. See paragraphs BC453A–BC453H.

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systems were in place to capture the information that would be required to apply IFRS 15 retrospectively. Some respondents further explained that because of the large volume of contracts in their businesses, it would be far more cost-effective to process the information on a real-time basis to ensure that the adjustments to the financial statements were being calculated during the transition period, rather than attempting to retrospectively calculate the adjustments at the date of initial application.

BC448 The boards considered whether their decision to permit an alternative transition method (see paragraphs BC439–BC444) would provide sufficient relief that an effective date of 1 January 2016, would be appropriate. However, the boards noted that if a contract is not completed at the date of initial application, the entity would need to apply IFRS 15 to that entire contract to calculate any cumulative effect that would be recognised in the opening retained earnings in the year of initial application. The boards noted that the industries that would be most affected generally have contracts with durations that would result in those industries still having only a few months to prepare their processes and systems to capture the required information on a real-time basis.

BC449 Consequently, the FASB decided to require that a public entity apply Topic 606 for annual reporting periods beginning after 15 December 2016, and the IASB decided to require that an entity apply IFRS 15 for annual reporting periods beginning on or after 1 January 2017. Although the effective dates are not identical, the boards noted that this difference has resulted from precedents in IFRS and US GAAP. Furthermore, the difference is not significant and the boards did not expect that it would result in a difference in the way that an entity considers the effective date.

BC450 The boards acknowledged that the period of time from which IFRS 15 is issued until its effective date is longer than usual. However, in this case, the boards decided that a delayed effective date is appropriate because of the unique attributes of IFRS 15, including the wide range of entities that will be affected and the potentially significant effect that a change in revenue recognition has on other financial statement line items.

BC451 To ensure consistency with the IASB's requirements in IAS 34, the FASB clarified that the first set of interim financial reports in which Topic 606 will apply is the first set of interim financial reports after the effective date (ie 31 March 2017 for a calendar year-end entity). The FASB also decided that this is appropriate because of the relatively long lead time that has been provided to entities.

Early application

BC452 The FASB decided not to allow entities to apply Topic 606 early, because doing so would have reduced the comparability of financial reporting in the period up to the date of initial application.¹² Although the IASB agreed that allowing early application would reduce the comparability of financial reporting in the

¹² The FASB subsequently amended Topic 606 to allow all entities to apply the Standard early for annual periods beginning after 15 December 2016. See paragraph BC453H.

period up to the date of initial application, the IASB noted that IFRS 15 improves accounting for revenue in areas in which there was little guidance under previous revenue Standards in IFRS and, thus, entities should not be precluded from applying IFRS 15 before its effective date. Furthermore, the IASB noted that IFRS 15 should resolve some pressing issues in practice arising from previous revenue recognition requirements. For example, the requirements for determining whether a performance obligation is satisfied over time should address the current diversity in practice associated with the application of the interpretation of IFRS on the construction of real estate.

- BC453 The boards observed that the IASB-only decision to permit early application should not result in differences after the date of initial application in the accounting for revenue between entities applying US GAAP and those applying IFRS that apply IFRS 15 early, even for contracts that straddle the date of initial application.

Deferral of effective date (amendment issued in September 2015)

- BC453A After issuing IFRS 15 and Topic 606, the IASB and the FASB formed a joint Transition Resource Group (TRG) for Revenue Recognition to support the implementation of the Standard. The TRG discussed submissions from stakeholders and its discussions on five topics indicated potential differences of views on how to implement the requirements in IFRS 15. Consequently, those topics were discussed by the boards and each board decided to propose targeted amendments to IFRS 15 and Topic 606. The IASB published an Exposure Draft *Clarifications to IFRS 15* in July 2015. In the light of those proposed amendments, the IASB and the FASB each discussed whether to defer the effective date of the Standard.
- BC453B The IASB observed that changing the effective date of a Standard shortly after its issuance creates uncertainty for stakeholders and has the potential to set a bad precedent. The effective date is set after consideration of information obtained in the exposure process about the time needed to implement the requirements. Accordingly, the IASB would consider changing the effective date only in exceptional circumstances. The IASB noted that it had already provided a considerable amount of time between issuing IFRS 15 and the effective date, anticipating that some entities would be required to change information technology systems and processes when applying the Standard. The IASB has also provided substantive relief on transition to IFRS 15 by giving entities a choice of transition methods, one of which does not involve the restatement of comparative financial information. In addition, the IASB observed that the proposed amendments noted in paragraph BC453A are expected to clarify, rather than change, the requirements of the Standard.
- BC453C Nonetheless, the IASB decided to propose a deferral of the effective date of IFRS 15 by one year to 1 January 2018 because of the combination of the following factors that result in the circumstances surrounding the implementation of IFRS 15 being exceptional:

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- (a) The IASB acknowledged that, although intended to provide clarity, the proposed amendments to IFRS 15 noted in paragraph BC453A may affect some entities that would wish to apply any amendments at the same time as they first apply IFRS 15. Those entities are likely to wish to avoid reporting changes to revenue when first implementing the Standard and then, within a year or two, potentially reporting further changes to revenue as a result of applying any amendments to the Standard. For those entities, a deferral of the effective date by one year would provide additional time to implement any amendments to the Standard.
- (b) IFRS 15 was issued later than had been anticipated when the IASB set the effective date of the Standard, which absorbed some of the implementation time that entities were expecting to have.
- (c) IFRS 15 is a converged Standard with Topic 606—although this was not the only consideration, the IASB observed that there are benefits for a broad range of stakeholders of retaining an effective date that is aligned with the effective date of Topic 606.

BC453D Accordingly, the IASB published the Exposure Draft *Effective Date of IFRS 15* in May 2015 proposing to defer the effective date of IFRS 15 by one year.

BC453E The IASB concluded that a one-year deferral would be sufficient in terms of providing additional time to implement IFRS 15. IASB members observed that the issuance of IFRS 15 in May 2014 had been later than anticipated by some months, not years. Accordingly, a deferral of the effective date of IFRS 15 for anything longer than one year would unnecessarily delay transition by many entities to a new Standard that the IASB views as a substantial improvement to financial reporting.

BC453F Almost all respondents to the Exposure Draft agreed with the proposal to defer the effective date of IFRS 15 for one or more of the reasons noted by the IASB, some noting the exceptional nature of the circumstances surrounding the implementation of IFRS 15. Most also agreed that a one-year deferral should be sufficient and would improve the quality of implementation.

BC453G In the light of the feedback received, the IASB confirmed its decision to defer the effective date of the Standard. The IASB did not change its previous decision to permit early application of IFRS 15.

BC453H For factors similar to those considered by the IASB, the FASB issued an Accounting Standards Update 2015-14 *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date* in August 2015 also deferring the effective date of Topic 606 for all entities by one year. Consequently, a public entity would be required to apply Topic 606 to annual reporting periods beginning after 15 December 2017. The FASB decided to permit early application of Topic 606 by all entities, but not before the original effective date of Topic 606 for a public entity (ie annual reporting periods beginning after 15 December 2016).

Clarifications to IFRS 15 (amendments issued in April 2016)

- BC453I As explained in paragraph BC453C, one of the considerations of the IASB in deferring the effective date of IFRS 15 from 1 January 2017 to 1 January 2018 was that the deferral would provide additional time to entities that wish to implement *Clarifications to IFRS 15* along with IFRS 15. Consequently, the IASB set an effective date for *Clarifications to IFRS 15* that aligns with the revised effective date of IFRS 15.
- BC453J Furthermore, the IASB decided that an entity should be permitted to apply *Clarifications to IFRS 15* earlier than its effective date. This would allow an entity the choice of either:
- (a) applying *Clarifications to IFRS 15* on the same date as it first applies IFRS 15; or
 - (b) applying *Clarifications to IFRS 15* at a date later than when it early applies IFRS 15.

In other words, an entity that has decided to early apply IFRS 15 would have the flexibility to apply *Clarifications to IFRS 15* either together with the Standard or at a subsequent date.

Analysis of the effects of IFRS 15

- BC454 The objective of financial statements is to provide information about the financial position, financial performance and cash flows of an entity that is useful to a wide range of users of financial statements in making economic decisions. To attain that objective, the boards try to ensure that new requirements meet a significant need and that the overall benefits to economic decision-making that would result from improved financial reporting justify the costs of providing such information. For example, the boards consider the comparative advantage that preparers have in developing information, compared with the costs that users of financial statements would incur to develop surrogate information. In this evaluation, the boards recognise that the costs of implementing a new standard might not be borne evenly by participants in the financial reporting system. However, both the users of financial statements and the entities that prepare those financial statements benefit from improvements in financial reporting that facilitate the functioning of markets for capital, including credit and the efficient allocation of resources in the economy.
- BC455 The IASB is committed to assessing and sharing knowledge about the likely costs of implementing new requirements and the likely, associated ongoing costs and benefits of each new Standard—these costs and benefits are collectively referred to as ‘effects’. The evaluation of these effects is necessarily subjective and qualitative. This is because quantifying costs and, particularly, benefits, is inherently difficult. Although other standard-setters undertake similar types of analyses, there is a lack of sufficiently well-established and reliable techniques for quantifying this analysis. Consequently, the IASB sees this analysis of the effects as being part of an evolving process. In addition, the assessment undertaken is that of the likely

effects of the new requirements because the actual effects would not be known until after the new requirements had been applied. These are subsequently analysed through the Post-implementation Review process.

Overview

- BC456 As explained in paragraphs BC2–BC3, the boards developed IFRS 15 to eliminate the inconsistencies and weaknesses in previous revenue recognition requirements and to improve disclosure requirements related to revenue. However, throughout the project, many preparers and some users of financial statements explained that they did not perceive significant weaknesses in previous revenue recognition requirements. Therefore, those preparers and users questioned whether the benefits of applying a new revenue standard would justify the costs of implementing that standard.
- BC457 To gain insight on the likely effects of IFRS 15, the boards conducted extensive consultation with interested parties through the formal exposure of the proposals and outreach activities. This consultation included three formal exposure documents—a Discussion Paper and two Exposure Drafts—in response to which the boards received and assessed more than 1,500 comment letters. Over the course of the project, the boards and staff also held more than 650 meetings with users of financial statements, preparers, auditors, regulators and other interested parties in a wide range of industries and a number of jurisdictions. Those meetings included general educational sessions about the proposals and in-depth discussions in relation to particular topics. Some meetings also focused on gaining an understanding of the effects of the proposals in specific industries or on particular transactions. In some cases, the boards undertook additional outreach in those specific industries or on those particular topics for which there were significant operational or other concerns about the effects of the boards' proposals. For example, because of the disparate views of preparers and users of financial statements on the topic of disclosure requirements, the boards sought further feedback in four workshops that brought user and preparer groups together to discuss how to balance the requirements to be more useful for users of financial statements and less burdensome for preparers (see paragraph BC328). In addition, because of the effect of the principles for allocating the transaction price on a typical mobile phone contract, the boards also held a number of meetings with representatives from the telecommunications industry to better understand their concerns and so that those concerns could be considered during redeliberations. The boards' consideration of the feedback received from this industry and their conclusions is included in paragraphs BC287–BC293 and BC473–BC476.
- BC458 The boards considered in their redeliberations all of the feedback received and, as a result, decided to modify or clarify many aspects of the revenue recognition model to reduce the burden of implementing and applying the proposed requirements. Discussion of this feedback and the resulting changes in different aspects of the model are included throughout the Basis for Conclusions and are summarised in this analysis of the effects.

- BC459 Overall, the boards concluded that the improvements to financial reporting would justify the costs of implementing IFRS 15. In making this assessment, the boards considered:
- (a) how revenue from contracts with customers would be reported in the financial statements;
 - (b) how the comparability of financial information would be improved and the benefit of better economic decision-making as a result of improved financial reporting;
 - (c) the likely compliance costs for preparers of financial statements; and
 - (d) the likely costs of analysis for users of financial statements.

Reporting revenue from contracts with customers in the financial statements

- BC460 IFRS 15 replaces the previous limited revenue recognition requirements in IFRS and the broad revenue recognition concepts and industry-specific requirements in US GAAP with a robust and comprehensive framework that is applied to all revenue contracts with customers (except for lease, insurance and financial instruments contracts which fall within the scope of other Standards). This framework provides a basis that should be more easily applied to complex transactions and that provides timely guidance for evolving revenue transactions.
- BC461 The framework in IFRS 15 also fills a gap by providing requirements for revenue transactions that had not previously been addressed comprehensively, such as transactions for revenue for the provision of services and for revenue resulting from licences of intellectual property. In addition, IFRS 15 provides requirements for issues such as contract modifications that were previously addressed only for a particular industry. IFRS 15 also provides improved requirements for some transactions such as multiple-element arrangements (see paragraphs BC470–BC472).
- BC462 By providing a comprehensive framework, one of the most significant effects of IFRS 15 in reporting revenue from contracts with customers is greater consistency in the accounting for economically similar transactions. This is because the diversity in practice that developed as a result of weaknesses in previous revenue recognition requirements in IFRS and US GAAP would be eliminated. However, the previous inconsistencies in the accounting and the diversity in practice that existed before the issuance of IFRS 15 may mean that the nature and extent of the changes would likely vary between entities and industries. For example, some industries, such as the telecommunications and software industries, may have significant changes. This is because those industries had narrow and transaction-specific industry revenue recognition requirements in US GAAP (which were often referred to by entities applying IFRS). However, other industries, such as the construction industry, may see minimal changes overall but significant changes for particular entities or jurisdictions that may have interpreted previous requirements differently to apply to their specific transactions. For other contracts, such as

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straightforward retail transactions, IFRS 15 would have little, if any, effect. The boards were aware of those varying effects when developing IFRS 15 and took them into account in their decision-making. In many cases, the boards observed that the requirements in IFRS 15 may be broadly consistent with previous revenue recognition requirements or practices, thus limiting the effects of IFRS 15 for many entities.

BC463 In making their assessment of the nature of the changes in the reporting of revenue from contracts with customers (ie the recognition and measurement of revenue), the boards observed that the following parts of the revenue recognition model are expected to result in the most significant changes for some entities:

- (a) transfer of control: basis for the timing of revenue recognition;
- (b) identification of performance obligations in a contract;
- (c) allocating the transaction price to performance obligations based on relative stand-alone selling prices; and
- (d) measurement of revenue.

Transfer of control: basis for the timing of revenue recognition

BC464 Previous revenue recognition requirements typically determined the timing of revenue recognition depending on whether the asset transferred was a good or a service. Both IFRS and US GAAP required revenue to be recognised for goods when risks and rewards transferred and, for services, as the service was performed. However, both approaches presented challenges in determining when to recognise revenue and often resulted in accounting for economically similar transactions differently. For example, when determining when to recognise revenue for the transfer of a good, it was often difficult for an entity to judge whether a preponderance (or some other balance) of the risks and rewards had been transferred to the customer. In some contracts, there could be significant difficulty in interpreting whether the asset to be transferred was a good or a service, therefore, making it difficult to rationalise why for one asset, revenue should be recognised only when the asset was complete (ie a good), whereas for another asset, revenue should be recognised continuously as that asset is created (ie a service). Some of this difficulty was due to the vague and narrow definition of services in US GAAP and the lack of clear rationale (ie a Basis for Conclusions) in IFRS for why, in some cases, revenue should be recognised for a service over time. In some cases, entities that applied IFRS consulted the rationale in US GAAP for why revenue would be recognised over time for a service. That rationale explained that this was because the entity was transferring a service continuously. However, that rationale did not address many specific application questions in IFRS about determining whether specific items met the definition of a service. In response, the IASB developed an Interpretation to help clarify whether the construction of real estate would be accounted for as a good or a service (ie a performance obligation satisfied at a point in time or over time). However, many observed that the principle in that Interpretation was difficult to understand and apply.

- BC465 In the light of the challenges with previous revenue recognition requirements, the boards observed that applying the single framework in IFRS 15 to determine the timing of revenue recognition for both goods *and* services would improve the consistency in accounting for revenue. This is because the framework would be applied to the attributes of the goods and services transferred, together with the terms of the contract, rather than only to the type of contract. In addition, the boards determined that the core principle in IFRS 15, based on the notion of transferring control, would further improve the consistency of reporting because it would provide a more objective assessment for determining the timing of revenue recognition.
- BC466 The boards noted that the application of the core principle may not result in changes for all contracts. For example, the boards acknowledge that for construction contracts, the application of the criteria for when a good or service transfers over time (and thus, is a performance obligation satisfied over time) in IFRS 15 would likely broadly result in the same accounting as required by previous revenue recognition requirements for contracts that met the definition of ‘services’. However, the boards observed that the application of IFRS 15 could result in changes for those contracts for which, under previous revenue recognition requirements, it may have been difficult to conclude that the contracted activities were services. This may occur in some manufacturing service contracts and contracts for the construction of residential real estate.

Application guidance: licensing

- BC467 Previous revenue recognition requirements did not determine the timing of revenue recognition for licences based on an assessment of whether the licence was a good or a service. However, those previous requirements were limited and industry-specific. For example, in US GAAP, revenue recognition for licences differed depending on the industry (for example, franchisors, media and entertainment and software) and often was based on features of the licence (for example, licence period or payment terms). Therefore, the previous revenue recognition requirements did not coalesce into a single principle or rule. In IFRS, previous revenue recognition requirements for licences required revenue to be recognised ‘in accordance with the substance of the agreement’. However, because those requirements provided minimal guidance on how an entity should assess the ‘substance of the agreement’, there was significant diversity in practice for the accounting for licences.
- BC468 The boards included in IFRS 15 application guidance on how an entity should assess and account for its licence arrangements. That guidance is anchored in applying key steps of the revenue recognition model—specifically, identifying the performance obligations in a contract and assessing the transfer of control, which the boards operationalised by differentiating between two types of licences. The boards also decided to include in the application guidance the rationale for the guidance and additional illustrative examples to explain the intention, objective and application of those steps and the differentiation between licences.

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BC469 The detailed application guidance for licences in IFRS 15 is intended to help entities determine when a licence is transferred to a customer and thus when revenue can be recognised. Because of the previous diversity in practice in revenue recognition for licences, the addition of the application guidance in IFRS 15 may change practice for some entities. However, the boards observed that the diversity and inconsistencies that previously existed meant that some changes in practice would have occurred regardless of how the boards decided to apply the revenue recognition model to licences.

Identification of performance obligations in a contract

BC470 The boards cited deficiencies in previous IFRS and US GAAP in the accounting for arrangements with multiple elements as one of the reasons for adding the Revenue Recognition project to its agenda. Although US GAAP was improved after the Revenue Recognition project began, deficiencies still existed. For example, there was no definition of a 'deliverable' in previous US GAAP, even though the term was used to determine the unit of account for revenue transactions. IFRS had even fewer requirements because it only acknowledged that revenue could be recognised for 'separately identifiable components of a single transaction', without providing guidance on how to determine what constituted a 'separately identifiable component'.

BC471 IFRS 15 addresses those weaknesses by defining promised goods or services that should be accounted for separately as performance obligations. IFRS 15 defines a performance obligation and provides criteria and factors for identifying performance obligations, which are based on the notion of distinct goods or services. These requirements were developed on the basis of extensive consultation and attempts to separate contracts in a meaningful and cost-effective way with intuitive outcomes.

BC472 The boards observed that the requirements in IFRS 15 for identifying performance obligations may not result in significant changes for many entities. This is because many entities have developed practices to separate contracts with customers in a manner that was similar to the requirements in IFRS 15. However, the boards observed that because there were specific requirements in previous US GAAP, there would be a change in the accounting for incidental obligations and marketing incentives (see paragraphs BC87–BC93). This is because the requirements in IFRS 15 would require an entity to identify and recognise revenue for those goods or services, when previously they may have been recognised as an expense or ignored for the purposes of revenue recognition. The boards observed that two industries that would be particularly affected by this change are the automotive industry (which previously recognised as an expense the promise of maintenance with the purchase of an automobile) and the telecommunications industry (which sometimes did not attribute any revenue to the handsets provided as part of a bundled offering).

Allocating the transaction price to performance obligations based on relative stand-alone selling prices

- BC473 Previous revenue recognition requirements in IFRS and US GAAP for the allocation of consideration in multiple-element arrangements were different. Before IFRS 15, there were no general requirements in IFRS for allocation of consideration (there were some specific requirements in an Interpretation for one type of transaction – that is, customer loyalty points). This was due in part to the lack of guidance on defining an element or unit of account for revenue. In contrast, US GAAP specified that an allocation of the consideration to multiple-elements should be made on a relative selling price basis for some industries. US GAAP also included explicit requirements for some industries on determining the selling price of an item, which required an entity to use vendor-specific objective evidence, but it also permitted the use of estimation techniques in some cases. However, the allocation requirements in the software industry strictly prohibited allocation to individual elements unless the entity obtained vendor-specific objective evidence for all elements of the contract. Because there was often no vendor-specific objective evidence available for one or more undelivered elements, revenue recognition was delayed until all elements had been delivered.
- BC474 Although the principle for allocating the transaction price in IFRS 15 is broadly consistent with previous US GAAP for some industries – that is, allocating the transaction price on a relative stand-alone selling price basis – there may be a change in some outcomes, in particular in the software industry. This is because the boards decided to eliminate the restrictive, industry-specific requirements in US GAAP for allocating consideration in software arrangements (ie the requirement to have vendor-specific objective evidence for all elements in the arrangements before consideration can be allocated). Instead, IFRS 15 requires an entity to estimate the stand-alone selling price of a good or service, if the stand-alone selling price is not directly observable. The boards observed that this change would permit an entity in the software industry to better depict performance by recognising revenue for performance obligations when they are satisfied, instead of when all performance in a contract is complete. In some instances, the boards observed that this may permit entities to eliminate the disclosure of non-GAAP measures that were created because the outcomes from applying previous revenue recognition requirements did not faithfully depict an entity's performance.
- BC475 The boards observed that the requirements for allocating the transaction price in IFRS 15, in conjunction with the requirements for identifying performance obligations, may also result in a significant change in the accounting for bundled arrangements in the automotive and telecommunications industries. As explained in paragraph BC457, the boards' consideration of the feedback received from the telecommunications industry and their conclusions are included in paragraphs BC287–BC293.

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BC476 The boards observed that even though IFRS 15 may result in significant differences in the allocation of the transaction price to performance obligations (and consequently in the amount and timing of the recognition of revenue) in some industries, the change was necessary to provide greater consistency in the recognition of revenue across industries. In addition, the boards observed that the effects were a consequence of the boards' objectives of eliminating industry-specific requirements and defining a common framework that could be applied to all revenue transactions. Furthermore, the boards observed that the allocation requirements in IFRS 15 would result in accounting for a transaction in a manner that more closely reflects the underlying economics.

Measurement of revenue

BC477 Previous requirements for the measurement of revenue in US GAAP were limited and differed for goods and for services. US GAAP did not provide specific requirements for how to measure revenue for goods, but it nevertheless restricted the amount of revenue that could be recognised for goods to the amount that was fixed or determinable. IFRS required revenue to be recognised for the transfer of goods and services at the fair value of the consideration received/receivable; but, there was no guidance on how to apply that principle because IFRS 13 *Fair Value Measurement* was not effective until 1 January 2013. Consequently, that principle was not consistently applied. In addition, IFRS contained little guidance on how to measure variable consideration. However, both IFRS and US GAAP indicated that the amount of revenue to be recognised for services should be limited to an amount that could be 'estimated reliably'.

BC478 Thus, IFRS 15 appears to be a significant change from previous revenue recognition requirements because it introduces a customer consideration model and measures revenue using the transaction price, which is defined as the amount to which the entity expects to be entitled in exchange for transferring goods or services. However, previous practices were broadly consistent with this approach and many entities determined the amount of revenue on the basis of the amounts the customer promised to pay. Where IFRS 15 differs from previous revenue recognition requirements is in the additional guidance it provides for estimating consideration when it is variable and in constraining those estimates to ensure revenue is not overstated. In addition, IFRS 15 provides requirements related to other aspects of measuring revenue such as accounting for significant financing components, non-cash consideration and consideration payable to a customer.

BC479 The additional guidance includes two methods for estimating variable consideration, which may not substantially change the amount of revenue recognised in many industries in which robust estimation methods have been developed over time. However, it may result in changes in the timing of revenue recognised in other cases, for which estimation of variable consideration was either prohibited or not used in the recognition of revenue. For example, in some distribution channels, entities may not have estimated the price of a good or service when that price depended on the eventual sale to an end customer. In those cases, revenue was not recognised until that final

sale occurred. The boards concluded that the additional guidance for estimation methods should ensure that performance is better reflected in the financial statements in those cases and should provide greater consistency in estimating variable consideration. The additional guidance would also provide users of financial statements with more transparency on the estimation process, which was often masked with undefined terms such as 'best estimates'.

- BC480 In addition, the requirements for constraining estimates of variable consideration provide entities with a more specific approach for assessing the likelihood of an entity being entitled to variable consideration and, therefore, whether or not to include an estimate of that variable consideration in the amount of revenue recognised. It would also give users of financial statements more confidence in the amount of revenue recognised in the financial statements by requiring a consistent approach to estimating the amount of variable consideration to which an entity is entitled. The boards included the requirements for constraining estimates of variable consideration in part because of feedback from users of financial statements who demanded that estimates should be of high quality, but also because a significant portion of errors in financial statements have related to the overstatement of revenue.

Improved comparability of financial information and better economic decision-making

- BC481 Before the issuance of IFRS 15, there were significant differences in accounting for economically similar revenue transactions, both within and across industries for entities applying US GAAP. There was also significant diversity in practice in accounting for revenue transactions for entities applying IFRS. Those differences made it difficult for users of financial statements to understand and compare revenue numbers. As explained in paragraphs BC460–BC480, some of this diversity arose because there were limited revenue recognition requirements in IFRS in general and on particular topics. Furthermore, the requirements that were provided were difficult to apply to complex transactions, in part because there was no rationale for those requirements (ie there was no Basis for Conclusions). Those differences also arose because previous revenue recognition requirements in US GAAP were voluminous and often industry-specific or transaction-specific, which also created difficulty for users of financial statements in interpreting the information about revenue. The boards noted that the diversity in practice and challenges to users were often amplified for entities applying IFRS because some preparers selectively referenced US GAAP.
- BC482 Analysis of revenue by users of financial statements was made even more difficult because previous disclosure requirements for revenue were inadequate. Consequently, users of financial statements found it difficult to understand an entity's revenues, as well as the judgements and estimates made by that entity in recognising those revenues. However, many entities acknowledged a need to provide investors with additional information about revenue and therefore provided this information in other reports outside the

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financial statements (for example, in earnings releases and shareholder reports).

BC483 By providing a robust, comprehensive framework that would be applied by entities applying both IFRS and US GAAP, IFRS 15 would eliminate the previous diversity in practice and create greater comparability across entities, industries and reporting periods. In addition, the boards observed that a common revenue Standard should make the financial reporting of revenue comparable between entities that prepare financial statements in accordance with IFRS or US GAAP, resulting in a significant benefit to users. Furthermore, by providing a rationale for the requirements (ie a Basis for Conclusions), the framework should be more easily applied to a broad range of transactions and contracts.

BC484 In addition, IFRS 15 provides comprehensive disclosure requirements that should greatly improve the information about revenue reported in the financial statements (see paragraphs BC327–BC361). Specifically, the information about revenue would enable users of financial statements to better understand an entity's contracts with customers and revenue from those contracts and to better predict cash flows. This information should also help users of financial statements to make more informed economic decisions. The boards acknowledged that these improvements may increase the costs of the application of IFRS 15 for preparers. However, the boards concluded that these costs were necessary to improve the usefulness of financial reporting in an area that is critical for users of financial statements to the analysis and understanding of an entity's performance and prospects.

BC485 During outreach, the boards learned that the disclosures required by IFRS 15 may help some entities to eliminate various alternative reporting measures that were created because previous revenue recognition requirements did not adequately depict their performance. Conversely, the boards noted that other industries in which changes may be more significant may be required to create alternative performance measures to help users understand the difference between previous accounting requirements and the requirements under IFRS 15. However, because the requirements adequately depict performance, the boards do not expect that these performance measures would be necessary in the longer term.

Compliance costs for preparers

BC486 As with any new requirements, there will be costs to implement IFRS 15. The breadth of industries and entities that will be required to apply IFRS 15, and the diversity in practice that existed under previous revenue recognition requirements, make it difficult to generalise the costs to preparers. However, because of the breadth of industries and entities that will be affected, most entities will incur at least some costs. Broadly, the boards expect that a majority of preparers may incur the following costs:

- (a) costs to implement changes in or develop new systems, processes and controls used to gather and archive contract data, make required estimates and provide required disclosures, possibly including fees paid to external consultants;
- (b) costs to hire additional employees that may be needed to comply with IFRS 15 and modify processes and internal controls accordingly;
- (c) incremental fees paid to external auditors to audit the financial statements in the period of initial application of IFRS 15;
- (d) costs required to educate management, finance and other personnel about the effects of IFRS 15; and
- (e) costs required to educate users of financial statements about the effects on the financial statements.

BC487 Many of the costs listed in paragraph BC486 will be non-recurring, because they will be incurred only upon initial application of IFRS 15. However, some entities that expect significant changes as a result of applying IFRS 15 expect that the continued application of IFRS 15 will likely cause the following long-term increases in costs:

- (a) increase in audit fees because of the increased volume of disclosures and the difficulty of auditing some of the required estimates (for example, estimates of stand-alone selling price and variable consideration);
- (b) costs to maintain improved systems and make modifications for transactions; and
- (c) higher personnel costs.

BC488 The boards considered those costs in their analysis of the effects for the Standard as a whole and in relation to specific provisions in IFRS 15 when making their decisions. Board members and staff consulted extensively across a wide range of industries and jurisdictions to better understand some of the operational issues arising from the proposals in the Discussion Paper and both Exposure Drafts. The boards took that feedback into consideration in their redeliberations and, as a result, modified or clarified many aspects of the revenue recognition model to reduce the burden of implementing and applying the requirements. Those decisions and their rationale are documented throughout the Basis for Conclusions in relation to specific aspects of the model such as variable consideration and significant financing components. Those clarifications and modifications included:

- (a) clarifying the use of portfolios – the boards clarified that many entities would not need to develop systems to account for each contract individually, especially entities that have a large volume of similar contracts with similar classes of customer. In those cases, the boards noted that entities may apply the requirements to a portfolio of similar contracts.

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- (b) practical expedients—the boards added some practical expedients (for example, in the requirements for adjusting the transaction price for significant financing components) to simplify compliance with the requirements in circumstances in which the boards determined that applying the practical expedient would have a limited effect on the amount or timing of revenue recognition.
- (c) disclosure requirements—the boards eliminated the rigidity in the disclosure requirements proposed in the 2011 Exposure Draft that required entities to provide a detailed reconciliation of their contract balances. Instead, the boards decided to require only the opening and closing balances as well as some information on the changes in those balances. The boards also provided similar relief for the reconciliation proposed in the 2011 Exposure Draft for the costs to obtain or fulfil a contract.
- (d) transition requirements—the boards expected that the costs of the systems and operational changes would be incurred primarily during the transition from previous revenue recognition requirements to IFRS 15. Therefore, to ease implementation costs and complexities associated with transition to IFRS 15, the boards decided to provide practical expedients that an entity may elect to use when applying the requirements retrospectively. In addition, the boards introduced an alternative transition method (ie the cumulative catch-up transition method) that would alleviate the costs of transition for many entities because it would not require restatement of prior periods.
- (e) additional illustrations—the boards responded to requests from respondents to provide examples that would illustrate the various aspects of IFRS 15 by providing educational guidance designed to help with implementation and understandability wherever possible. The boards concluded that this would help to reduce both the initial and ongoing cost of compliance, as well as enhancing the consistency of application and therefore comparability of financial statements.

Costs of analysis for users of financial statements

BC489 The boards note that, as with all new requirements, there will be an educational and adjustment period for users of financial statements, during which they may incur costs. Those costs may include costs to modify their processes and analyses. However, the costs are likely to be non-recurring and are likely to be offset by a longer-term reduction in costs from the additional information that would be provided by the improved disclosure requirements. Users of financial statements may also observe a longer-term reduction in education costs, because of the common framework created by IFRS 15, which applies across jurisdictions, industries and transactions.

BC490 In the boards' view, the significant benefits to users of financial statements from IFRS 15 will justify the costs that the users may incur. Those benefits include:

- (a) greater comparability and consistency of reporting revenue from contracts with customers;
- (b) a better depiction of entities' performance; and
- (c) improved understanding of entities' contracts and revenue-generating activities.

Conclusion

BC491 The boards concluded that the issuance of IFRS 15¹³ achieves their objectives as outlined in paragraph BC3. This is because IFRS 15 provides a robust and comprehensive framework that:

- (a) will apply to a broad range of transactions and industries and will improve the comparability of the recognition of revenue across industries and jurisdictions;
- (b) can be applied to complex transactions and evolving transactions, resulting in greater consistency in the recognition of revenue; and
- (c) will require enhanced disclosures that will improve the understandability of revenue, which is a critical part of the analysis of an entity's performance and prospects.

BC492 In the light of these achievements, the boards determined that the issuance of IFRS 15 would result in an overall improvement to financial reporting. The boards also concluded that these benefits would be ongoing and would justify the costs of implementing IFRS 15 (for example, systems and operational changes) that would be incurred primarily during the transition from previous revenue recognition requirements.

BC493 However, because of differences in their previous revenue recognition requirements, the boards noted that their rationale for the conclusion that IFRS 15 results in 'an improvement to financial reporting' was slightly different. The differences in their rationale are as follows:

- (a) Previous revenue recognition requirements in US GAAP were rules-based and provided specific requirements for particular transactions and industries. In addition, there were transactions that were not directly in the scope of specific guidance. Consequently, economically similar transactions were often accounted for differently. Overall, the robust and comprehensive framework in Topic 606 should improve comparability in the accounting for economically similar transactions and should result in accounting that better reflects the economics of those transactions.

¹³ As indicated in footnote 1, unless indicated otherwise, all references to IFRS 15 in this Basis for Conclusions can be read as also referring to Topic 606 in the FASB's Accounting Standards Codification.

- (b) As described in paragraph BC460, the previous revenue recognition requirements in IFRS were limited. In particular, IFRS did not include general requirements related to many key issues in revenue recognition such as multiple-element arrangements and how to allocate consideration to those elements. In addition, the lack of a Basis for Conclusions in those previous revenue recognition requirements in IFRS created challenges in assessing how to apply the principles in those requirements. In combination, these factors contributed to diversity in practice across jurisdictions and industries. By providing a comprehensive framework and a Basis for Conclusions, IFRS 15 should be a significant improvement to the previous revenue recognition requirements. Consequently, IFRS 15 should eliminate that previous diversity in practice and thus improve financial reporting.

Consequential amendments

Sales of assets that are not an output of an entity's ordinary activities

- BC494 For the transfer of non-financial assets that are not an output of an entity's ordinary activities, the boards decided to amend their respective Standards to require that an entity apply the requirements from IFRS 15 for the following topics:
- (a) control—to determine when to derecognise the asset.
 - (b) measurement—to determine the amount of the gain or loss to recognise when the asset is derecognised (including any constraints on the transaction price because it is variable).
- BC495 The FASB also decided to apply the requirements from Topic 606 for the existence of a contract to transfer a non-financial asset. Those requirements require an entity to determine whether the parties are committed to perform under the contract, which can be difficult in sales of real estate in which the seller has provided significant financing to the purchaser.
- BC496 Those amendments will result in changes to IAS 16 *Property, Plant and Equipment*, IAS 38 and IAS 40 *Investment Property* and to Topic 360 and Topic 350 *Intangibles—Goodwill and Other*. The changes to those Standards will result in the same accounting requirements under IFRS and US GAAP for the transfer of non-financial assets that are not an output of an entity's ordinary activities. However, because the requirements in those Standards were previously different under IFRS and US GAAP, the boards have different reasons for making those changes.

Consequential amendments to US GAAP

- BC497 A contract for the sale of real estate that is an output of an entity's ordinary activities meets the definition of a contract with a customer and, therefore, is within the scope of Topic 606. Because Subtopic 360-20 *Real Estate Sales* provided requirements for recognising profit on *all* real estate sales, regardless of whether real estate is an output of an entity's ordinary activities, the FASB

considered the implications of retaining the requirements in Subtopic 360-20 for contracts that are not within the scope of Topic 606. The FASB noted that retaining those requirements could result in an entity recognising the profit or loss on a real estate sale differently, depending on whether the transaction is a contract with a customer. However, there is economically little difference between the sale of real estate that is an output of the entity's ordinary activities and the sale of real estate that is not. Consequently, the difference in accounting should relate only to the presentation of the profit or loss in the statement of comprehensive income—revenue and expense or gain or loss.

- BC498 Consequently, the FASB decided to amend Topic 360 and create Subtopic 610-20 *Gains and Losses from the Derecognition of Nonfinancial Assets* to require that an entity apply the requirements in Topic 606 for the existence of a contract, for control, and for measurement of a contract for the transfer of real estate (including in-substance real estate) that is not an output of the entity's ordinary activities. If the real estate is a business (and not an in-substance non-financial asset), the requirements in Subtopic 810-10 for consolidation apply.
- BC499 The FASB also decided to specify that an entity apply the requirements in Topic 606 for the existence of a contract, for control and for measurement to contracts for the transfer of all non-financial assets in non-revenue transactions, such as tangible assets within the scope of Topic 360 and intangible assets within the scope of Topic 350. The primary reason for that decision was the lack of clear requirements in US GAAP for accounting for the transfer of non-financial assets when those assets are not an output of an entity's ordinary activities and do not constitute a business or non-profit activity. In addition, the FASB decided, due to the lack of guidance in Topics 350 and 360, to add guidance for how to account for a contract that fails to meet the criteria in paragraph 606-10-25-1.

Consequential amendments to IFRS

- BC500 In IFRS, an entity selling an asset within the scope of IAS 16, IAS 38 or IAS 40 would have applied the recognition principles of the previous revenue Standards in IFRS to determine when to derecognise the asset and, in determining the gain or loss on the transfer, would have measured the consideration at fair value. However, the IASB noted that there is diversity in practice in the recognition of the gain or loss when the transfer of those assets involves variable consideration, because the previous revenue Standard in IFRS did not provide specific requirements for variable consideration. The IASB decided that requiring application of the requirements in IFRS 15 for control and for measurement (including constraining the amount of variable consideration used in determining the gain or loss) would eliminate the diversity in practice because the requirements in IFRS 15 provide a clear principle for accounting for variable consideration.
- BC501 The IASB considered whether it should retain fair value as the measurement basis for transfers of non-financial assets within the scope of IAS 16, IAS 38 and IAS 40. However, the IASB rejected this proposal and, as explained in paragraph BC500, decided to require that an entity apply the measurement

requirements in IFRS 15 to transfers of non-financial assets that are not an output of the entity's ordinary activities, for the following reasons:

- (a) measuring the gain on the transfers of non-financial assets that are not an output of the entity's ordinary activities by using the same requirements as for measuring revenue provides users of financial statements with useful information. The IASB decided that it would provide useful information if entities apply the requirements for constraining estimates of variable consideration to any gain that will be recognised on the transfer of the non-financial asset. The IASB acknowledged that in some cases this may result in a loss on the transfer when the transferred asset has a cost basis that is greater than the constrained consideration, which may occur when the asset has a cost basis that is determined using fair value. However, the IASB noted that this outcome is appropriate and useful to users, because of the significant uncertainty about the variable consideration. The IASB also noted that this outcome is consistent with the outcome in a transaction with a customer in which the variable consideration is constrained, but the entity has transferred control of the good or service to the customer.
- (b) it is not necessary to measure the gains on the transfers of non-financial assets to be consistent with other asset disposals, such as disposals of an entity, that are accounted for at fair value in accordance with other Standards (for example, IFRS 10). This is because transfers of non-financial assets that are not an output of an entity's ordinary activities are more like transfers of assets to customers, rather than other asset disposals.
- (c) applying the measurement requirements in IFRS 15 achieves consistency with US GAAP.

A separate project

BC502 The boards also considered whether they should consider the changes to the guidance on transfers of non-financial assets in a separate project. The boards noted that undertaking a separate project would mean that changes to existing Standards would not be made until that project had been completed and became effective. Because of the boards' other standard-setting priorities, and the time required to complete all relevant due process steps for issuing a standard, it might be several years before the existing requirements were replaced. The boards observed that the implications of not proceeding with the proposed consequential amendments would have been as follows:

- (a) for IFRS reporters, the IASB would have needed to amend IAS 16, IAS 38 and IAS 40 to include the revenue recognition criteria from previous revenue Standards in IFRS. This would have resulted in different recognition and measurement requirements for transfers of non-financial assets as compared to contracts with customers.

- (b) for US GAAP reporters, there would have been two sets of recognition and measurement requirements for real estate sales, depending on whether the transfer was with a customer. In addition, no specific requirements would have been provided in US GAAP for transfers of non-financial assets (other than real estate) within the scope of Subtopic 360-10 (for example, equipment) or Topic 350 (for example, intangible assets).

BC503 Consequently, the boards reaffirmed their decision in the 2011 Exposure Draft that consequential amendments should be made, because this results in consistency in the accounting for the transfers of non-financial assets between IFRS and US GAAP, addresses the lack of requirements for the accounting for transfers of non-financial assets in US GAAP and eliminates possible complexities that might result from retaining separate recognition criteria for transfers of non-financial assets in IFRS.

Transition for first-time adopters of IFRS

BC504 During redeliberations of the transition requirements, the IASB considered whether to amend IFRS 1 *First-time Adoption of International Financial Reporting Standards* to allow a first-time adopter of IFRS to use the same transition methods for adopting IFRS 15 as specified in paragraph C3 of IFRS 15 as follows:

- (a) retrospectively to each prior period presented in accordance with IAS 8, subject to the practical expedients in paragraph C5 of IFRS 15; and
- (b) retrospectively with the cumulative effect of initially applying IFRS 15 recognised at the date of initial application (for a first-time adopter of IFRS, this would be the entity's first IFRS reporting period) in accordance with paragraphs C7–C8 of IFRS 15.

BC505 The IASB decided that the practical expedients in paragraph C5 of IFRS 15 should also apply to a first-time adopter, because both first-time adopters and entities that already apply IFRS would face similar challenges. The IASB observed that IFRS 1 requires that the accounting policies effective at the end of the first IFRS reporting period are applied to all reporting periods from the date of transition to IFRS onwards. This is identical to retrospective application for entities already applying IFRS. Some IASB members also noted that in many jurisdictions that have not yet adopted IFRS, revenue standards are similar to current IFRS. In those jurisdictions, the starting point for transition for a first-time adopter will be similar to entities already applying IFRS.

BC506 The IASB also clarified that, for any of the practical expedients in paragraph C5 of IFRS 15 that the entity uses, the entity should apply that expedient consistently to all reporting periods presented and disclose which expedients have been used, together with the estimated effect of applying those expedients (see paragraph C6 of IFRS 15).

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- BC507 Paragraphs BC439–BC444 explain the boards' rationale for including an additional transition method in IFRS 15. That method requires an entity (that is not a first-time adopter of IFRS) to apply IFRS 15 retrospectively with the cumulative effect of initially applying IFRS 15 recognised in the current year (referred to as the 'cumulative catch-up' transition method). Using the cumulative catch-up transition method, an entity would apply the requirements retrospectively only to contracts that are not completed at the beginning of the date of initial application (which, if applied to a first-time adopter would be the entity's first IFRS reporting period).
- BC508 However, the IASB decided not to amend IFRS 1 to permit first-time adopters of IFRS to use the cumulative catch-up transition method because it is not consistent with the principles of IFRS 1. This is because it would eliminate comparability within a first-time adopter's first IFRS financial statements by providing relief from restating comparative years. The IASB also observed that the cumulative catch-up transition method may not reduce the burden of retrospective application because it would potentially require two separate reconciliations of equity—one for the transition to IFRS, which would be recognised in the earliest comparative period, and one for the transition to IFRS 15, which would be recognised at the beginning of the entity's first IFRS reporting period. This would not only be challenging for preparers, but might also be confusing for users of financial statements.
- BC509 Despite deciding not to amend IFRS 1 to allow first-time adopters to use the cumulative catch-up transition method, the IASB decided to amend IFRS 1 to provide an optional exemption for first-time adopters from the requirements of IFRS 15 in accounting for contracts completed before the earliest period presented. Under this exemption, a first-time adopter would not be required to restate all of its contracts for which it has recognised all of its revenue in accordance with its previous GAAP before the earliest period presented.

Summary of main changes from the 2011 Exposure Draft

- BC510 The main changes from the proposals in the 2011 Exposure Draft are as follows:
- (a) IFRS 15 includes additional requirements related to identifying a contract with a customer. Specifically, IFRS 15 includes an additional criterion that must be met before an entity can apply the requirements in IFRS 15 to a contract. This criterion in paragraph 9(e) of IFRS 15 requires an entity to conclude that it is probable that a customer will pay the consideration to which the entity will be entitled by assessing the customer's ability and intention to pay. In addition, IFRS 15 provides guidance for accounting for contracts that do not meet the specified criteria and thus cannot apply IFRS 15.
 - (b) IFRS 15 clarifies the objective of the requirements for constraining estimates of variable consideration and provides a level of confidence of 'highly probable' for determining when to include those estimates in the transaction price. This represents a change from the 2011 Exposure Draft, which specified that an entity could only

recognise revenue for estimates of variable consideration when an entity was 'reasonably assured' that it would be entitled to that amount.

- (c) IFRS 15 provides additional guidance on the allocation of the transaction price to performance obligations:
 - (i) the residual approach may be used for two or more goods or services with highly variable or uncertain stand-alone selling prices if at least one good or service has a stand-alone selling price that is not highly variable or uncertain; and
 - (ii) allocation of a discount among performance obligations should be done before using the residual approach to estimate the stand-alone selling price for a good or service with a highly variable or uncertain stand-alone selling price.
- (d) IFRS 15 carries forward from the 2011 Exposure Draft the principles related to identifying performance obligations in a contract and determining whether a performance obligation is satisfied over time. However, IFRS 15 clarifies those principles and provides additional guidance for entities in applying those principles.
- (e) IFRS 15 provides additional guidance for determining when a customer obtains control of a licence, by distinguishing between licences that provide a right to access the entity's intellectual property as it exists throughout the licence period and licences that provide a right to use the entity's intellectual property as it exists at the point in time at which the licence is granted. This determination will affect whether the entity satisfies its performance obligation to transfer a licence at a point in time or over time. This represents a change from the 2011 Exposure Draft, which specified that all licences were transferred to the customer at the point in time at which the customer obtained control of the rights. IFRS 15 also clarifies that before determining when the licence transfers to the customer, an entity considers the promises in the contract and applies the requirements for identifying performance obligations.
- (f) IFRS 15 does not include the requirements proposed in the 2011 Exposure Draft to test a performance obligation to determine whether it is onerous.
- (g) IFRS 15 clarifies the disclosures required for revenue from contracts with customers. Specifically, it requires an entity to provide a combination of qualitative and quantitative information about contract balances. The 2011 Exposure Draft required this disclosure to be provided as a reconciliation of contract balances.
- (h) IFRS 15 provides entities with an additional transition method that does not require a restatement of prior periods. The 2011 Exposure Draft proposed only one transition method (ie a retrospective transition method with practical expedients) that requires a restatement of all previous periods presented.

Dissenting Opinion

Dissenting Opinion from *Clarifications to IFRS 15 Revenue from Contracts with Customers* as issued in April 2016

- DO1 Mr Ochi voted against the publication of *Clarifications to IFRS 15 Revenue from Contracts with Customers*. He agrees with all of the clarifying amendments to IFRS 15 and the additional transition reliefs. However, he disagrees with the IASB's decision to require entities to apply *Clarifications to IFRS 15* retrospectively as if those amendments had been included in IFRS 15 at the date of initial application.
- DO2 Referring to the IASB's considerations explained in paragraph BC445T, he thinks that requiring an entity that has applied IFRS 15 before applying these amendments to restate the effects of initially applying IFRS 15 for the effects, if any, of initially applying the amendments is inconsistent with allowing early application of IFRS 15. That entity might be required to restate some contracts twice, first on initially applying IFRS 15 and again on initial application of these amendments. Furthermore, that entity is deprived of the benefit of the new practical expedients added by the IASB.
- DO3 Mr Ochi does not disagree with issuing clarifications, if absolutely necessary, to a Standard before its effective date. However, the IASB's actions in issuing any such clarifying amendments should not be perceived as penalising those entities that begin their implementation process early and rewarding those that delay. Such perceptions could discourage entities from starting the implementation of any new Standard on a timely basis.
- DO4 Mr Ochi noted that the effective date of the new leases Standard has been set so as to provide a long initial implementation period. In that regard, he believes that allowing early application of a Standard supports the smooth application of new Standards.
- DO5 To encourage early application of Standards, he thinks that the IASB should, when deciding the transition requirements for amendments such as *Clarifications to IFRS 15*, give due consideration to those entities that have already early applied the Standard or are in advanced stages of preparing to do so. When deciding the transition requirements, he thinks it is not just a question of considering the extent or potential effect of any clarifications to a Standard; rather it is a matter of principle.

Appendix A

Comparison of IFRS 15 and Topic 606¹⁴

- A1 IFRS 15, together with the FASB's Topic 606, issued in May 2014 completes a joint effort by the IASB and the FASB to improve financial reporting by creating a common revenue standard for IFRS and US GAAP that can be applied consistently across various transactions, industries and capital markets. In IFRS 15 and Topic 606, the boards achieved their goal of reaching the same conclusions on all requirements for the accounting for revenue from contracts with customers. However, there are some minor differences in the standards as issued in May 2014, which are as follows:
- (a) **Collectability threshold** – the boards included an explicit collectability threshold as one of the criteria that a contract must meet before an entity can recognise revenue. For a contract to meet that criterion, an entity must conclude that it is probable that it will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. In setting the threshold, the boards acknowledged that the term 'probable' has different meanings in IFRS and in US GAAP. However, the boards decided to set the threshold at a level that is consistent with previous revenue recognition practices and requirements in IFRS and in US GAAP. (See paragraphs BC42–BC46.)
 - (b) **Interim disclosure requirements** – the boards noted that the general principles in their respective interim reporting requirements (IAS 34 *Interim Financial Reporting* and Topic 270 *Interim Reporting*) would apply to revenue from contracts with customers. However, the IASB decided to also amend IAS 34 to specifically require the disclosure of disaggregated information of revenue from contracts with customers in interim financial reports. The FASB similarly decided to amend Topic 270, to require a public entity to disclose disaggregated revenue information in interim financial reports, but also made amendments to require information about both contract balances and remaining performance obligations to be disclosed on an interim basis. (See paragraphs BC358–BC361.)
 - (c) **Early application and effective date** – paragraph C1 of IFRS 15 allows entities to apply the requirements early, whereas Topic 606 prohibits a public entity from applying the requirements earlier than the effective date.¹⁵ In addition, the effective date for IFRS 15 is for annual reporting periods beginning on or after 1 January 2017, whereas Topic 606 has

¹⁴ This Appendix reflects the differences between IFRS 15 and Topic 606 when those standards were issued in May 2014 updated to reflect the issue of *Clarifications to IFRS 15* in April 2016.

¹⁵ The FASB subsequently amended Topic 606 in August 2015 to allow all entities to apply the standard early for annual periods beginning after 15 December 2016. See paragraph BC453H.

an effective date for public entities for annual reporting periods beginning after 15 December 2016.¹⁶ (See paragraphs BC452–BC453.)

- (d) **Impairment loss reversal**—paragraph 104 of IFRS 15 requires an entity to reverse impairment losses, which is consistent with the requirements for the impairment of assets within the scope of IAS 36 *Impairment of Assets*. In contrast, consistent with other areas of US GAAP, Topic 606 does not allow an entity to reverse an impairment loss on an asset that is recognised in accordance with the guidance on costs to obtain or fulfil a contract. (See paragraphs BC309–BC311.)
- (e) **Non-public entity requirements**—there are no specific requirements included in IFRS 15 for non-public entities. Entities that do not have public accountability may apply *IFRS for Small and Medium-sized Entities*. Topic 606 applies to non-public entities, although some specific reliefs relating to disclosure, transition and effective date have been included in Topic 606 for non-public entities.

A1A As explained in paragraph BC1A, the IASB issued *Clarifications to IFRS 15* in April 2016, which differed in some respects from the amendments to Topic 606 issued by the FASB, and those expected to be issued by the FASB based on its decisions, until March 2016. The differences are as follows:

- (a) **Collectability criterion**—The FASB decided to amend paragraph 606-10-25-1(e) of Topic 606 (equivalent to paragraph 9(e) of IFRS 15), and add implementation guidance and illustrations to clarify that an entity should assess the collectability of the consideration promised in a contract for the goods or services that will be transferred to the customer rather than assessing the collectability of the consideration promised in the contract for all of the promised goods or services. The IASB did not make similar amendments to IFRS 15. (See paragraphs BC46B–BC46E.)
- (b) **Revenue recognition for contracts with customers that do not meet the Step 1 criteria**—The FASB decided to amend paragraph 606-10-25-7 of Topic 606 (equivalent to paragraph 15 of IFRS 15) to add an event in which an entity recognises any consideration received as revenue when (a) the entity has transferred control of the goods or services to which the consideration received relates; (b) the entity has stopped transferring additional goods or services and has no obligation to transfer additional goods or services; and (c) the consideration received from the customer is non-refundable. The IASB did not make similar amendments to IFRS 15. (See paragraphs BC46F–BC46H.)
- (c) **Promised goods or services that are immaterial within the context of the contract**—The FASB decided to amend Topic 606 to state that an entity is not required to assess whether promised goods or services are performance obligations if they are immaterial within the context of

¹⁶ The IASB issued *Effective Date of IFRS 15* in September 2015 deferring the effective date of IFRS 15 by one year. Similarly, the FASB amended Topic 606 in August 2015 deferring the effective date of Topic 606 by one year. See paragraphs BC453A–BC453H.

the contract with the customer. The IASB did not make similar amendments to IFRS 15. (See paragraphs BC116A–BC116E.)

- (d) **Shipping and handling activities**—The FASB decided to amend Topic 606 to permit an entity, as an accounting policy election, to account for shipping and handling activities that occur after the customer has obtained control of a good as fulfilment activities. The IASB decided not to make a similar amendment to IFRS 15. (See paragraphs BC116R–BC116U.)
- (e) **Presentation of sales taxes**—The FASB decided to amend Topic 606 to provide an accounting policy election that permits an entity to exclude from the measurement of the transaction price all taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction and collected from customers (for example, sales taxes, use taxes, value added taxes and some excise taxes). The IASB decided not to provide a similar accounting policy choice in IFRS 15. (See paragraphs BC188A–BC188D.)
- (f) **Non-cash consideration**—The FASB decided to amend Topic 606 to require non-cash consideration to be measured at its fair value at contract inception. The FASB also decided to specify that the constraint on variable consideration applies only to variability in the fair value of the non-cash consideration that arises for reasons other than the form of the consideration. The IASB did not make similar amendments to IFRS 15. (See paragraphs BC254A–BC254H.)
- (g) **Licensing**
 - (i) **Determining the nature of the entity’s promise in granting a licence of intellectual property**—IFRS 15 and Topic 606 require entities to determine whether the nature of an entity’s promise in granting a licence is a right to use or a right to access the entity’s intellectual property. The IASB did not amend the criteria in IFRS 15 to determine the nature of the licence but clarified that the assessment of whether the entity’s activities significantly change the intellectual property to which the customer has rights is based on whether those activities affect the intellectual property’s ability to provide benefit to the customer. The FASB decided to amend the criteria to determine the nature of the licence by requiring an entity to classify the intellectual property underlying the licence as functional or symbolic based on whether the intellectual property has significant stand-alone functionality. A licence to functional intellectual property is considered a right to use, while a licence to symbolic intellectual property is considered a right to access the underlying intellectual property. (See paragraphs BC414C–BC414N.)

- (ii) **Contractual restrictions in a licence and the identification of performance obligations**—The FASB decided to amend Topic 606 to clarify that the requirements about contractual restrictions of the nature described in paragraph B62 do not replace the requirement for the entity to identify the number of licences promised in the contract. The IASB did not make similar amendments to IFRS 15. (See paragraphs BC414O–BC414R.)
- (iii) **Renewals of licences of intellectual property**—The FASB decided to amend Topic 606 and provide an additional example to specify that the entity would generally not recognise revenue from the transfer of the renewal licence until the beginning of the licence renewal period. The IASB did not make similar amendments. (See paragraphs BC414S–BC414U.)
- (iv) **When to consider the nature of an entity’s promise in granting a licence**—The FASB decided to make amendments that explicitly state that an entity considers the nature of its promise in granting a licence when applying the general revenue recognition model to a single performance obligation that includes a licence and other goods or services. The IASB did not make similar amendments to IFRS 15. (See paragraphs BC414V–BC414Y.)
- (h) **Completed contracts**—The FASB decided to amend the definition of a completed contract to be a contract for which all (or substantially all) of the revenue was recognised in accordance with the previous revenue Standards. The IASB did not make a similar amendment to IFRS 15. (See paragraphs BC445C–BC445I.) Furthermore, the IASB added a practical expedient to allow an entity applying IFRS 15 in accordance with paragraph C3(a) not to restate contracts that are completed contracts at the beginning of the earliest period presented. The FASB decided not to provide the practical expedient. (See paragraphs BC445M–BC445N.)
- (i) **Date of application of the contract modifications practical expedient**—For an entity applying Topic 606 in accordance with paragraph 606-10-65-1(d)(2) (equivalent to paragraph C3(b) of IFRS 15), the FASB decided that the entity should apply the practical expedient at the date of initial application. However, the IASB decided that an entity applying IFRS 15 in accordance with paragraph C3(b) may apply the practical expedient either (a) at the beginning of the earliest period presented; or (b) at the date of initial application. (See paragraphs BC445O–BC445R.)

A2 IFRS 15 and Topic 606 have been structured to be consistent with the style of other Standards in IFRS and US GAAP (respectively). As a result, the paragraph numbers of IFRS 15 and Topic 606 are not the same. The wording in most of the paragraphs is consistent because IFRS 15 and Topic 606 were issued in May 2014 as a common revenue standard for IFRS and US GAAP. However, the

wording in some paragraphs differs because of the different amendments to IFRS 15 and Topic 606 (see paragraph A1A). The following table illustrates how the paragraphs of IFRS 15 and Topic 606, and the related illustrative examples, correspond. Paragraphs in which the wording differs are marked with “*”. The table reflects amendments issued by the FASB, and those expected to be issued by the FASB based on its decisions, until March 2016.

IASB	FASB
MAIN FEATURES	OVERVIEW AND BACKGROUND
N/A	606-10-05-1
IN7	606-10-05-2
IN8	606-10-05-3
	606-10-05-4
IN9	606-10-05-5
N/A	606-10-05-6
OBJECTIVE	
1	606-10-10-1
Meeting the Objective	
2	606-10-10-2
3	606-10-10-3
4	606-10-10-4
SCOPE	
Entities	
N/A	606-10-15-1
Transactions	
5	606-10-15-2
6	606-10-15-3
7	606-10-15-4
8	606-10-15-5

IFRS 15 BC

RECOGNITION	
Identifying the Contract	
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13	606-10-25-5
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16	606-10-25-8
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17	606-10-25-9
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18	606-10-25-10
19	606-10-25-11
20	606-10-25-12
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23	606-10-25-15
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24	606-10-25-16*
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25	606-10-25-17*
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26	606-10-25-18
N/A	606-10-25-18A through 25-18B*
27	606-10-25-19
28	606-10-25-20
29	606-10-25-21
30	606-10-25-22

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35	606-10-25-27
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37	606-10-25-29
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40	606-10-25-32
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N/A	606-10-32-2A*
48	606-10-32-3
49	606-10-32-4

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51	606-10-32-6
52	606-10-32-7
53	606-10-32-8
54	606-10-32-9
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55	606-10-32-10
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56	606-10-32-11
57	606-10-32-12
58	606-10-32-13
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61	606-10-32-16
62	606-10-32-17
63	606-10-32-18
64	606-10-32-19
65	606-10-32-20
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67	606-10-32-22
68	606-10-32-23*
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71	606-10-32-26
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N/A	340-40-05-2
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94	340-40-25-4
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IE253	606-10-55-339
Example 50—Option That Does Not Provide the Customer with a Material Right (Additional Goods or Services)	
IE254	606-10-55-340
IE255	606-10-55-341
IE256	606-10-55-342
Example 51—Option That Provides the Customer with a Material Right (Renewal Option)	
IE257	606-10-55-343
IE258	606-10-55-344
IE259	606-10-55-345
IE260	606-10-55-346
IE261	606-10-55-347
IE262	606-10-55-348
IE263	606-10-55-349
IE264	606-10-55-350
IE265	606-10-55-351
IE266	606-10-55-352
Example 52—Customer Loyalty Programme	
IE267	606-10-55-353
IE268	606-10-55-354
IE269	606-10-55-355
IE270	606-10-55-356

NON-REFUNDABLE UPFRONT FEES	
IE271	606-10-55-357
Example 53—Non-refundable Upfront Fee	
IE272	606-10-55-358
IE273	606-10-55-359
IE274	606-10-55-360

LICENSING	
IE275	606-10-55-361*
Example 54—Right to Use Intellectual Property	
IE276	606-10-55-362
IE277	606-10-55-363 through 55-363B*
Example 55—Licence of Intellectual Property	
IE278	606-10-55-364
IE279	606-10-55-365
IE279A	606-10-55-365A
IE280	606-10-55-366*
Example 56—Identifying a Distinct Licence	
IE281	606-10-55-367*
IE282	606-10-55-368*
IE283	606-10-55-369
IE284	606-10-55-370*
IE285	606-10-55-371
IE286	606-10-55-372
IE286A	606-10-55-372A
IE287	606-10-55-373*
IE288	606-10-55-374*

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LICENSING	
Example 57—Franchise Rights	
IE289	606-10-55-375*
IE290	606-10-55-376*
IE291	606-10-55-377
IE292	606-10-55-378*
IE293	606-10-55-379*
IE294	606-10-55-380*
IE295	606-10-55-381*
IE296	606-10-55-382*
Example 58—Access to Intellectual Property	
IE297	606-10-55-383*
IE298	606-10-55-384
IE299	606-10-55-385*
IE300	606-10-55-386*
IE301	606-10-55-387*
IE302	606-10-55-388*
Example 59—Right to Use Intellectual Property	
IE303	606-10-55-389
IE304	606-10-55-390
IE305	606-10-55-391*
IE306	606-10-55-392*
N/A	606-10-55-392A through 55-392D*
Example 60—Sales-based royalty for a licence of intellectual property	
IE307	606-10-55-393
IE308	606-10-55-394
Example 61—Access to Intellectual Property	
IE309	606-10-55-395
IE310	606-10-55-396*
IE311	606-10-55-397*
IE312	606-10-55-398*
IE313	606-10-55-399*
Example 61A—Right to Use Intellectual Property	
N/A	606-10-55-399A through 55-399J*

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LICENSING	
Example 61B—Distinguishing Multiple Licences from Attributes of a Single Licence	
N/A	606-10-55-399K through 55-399O*

REPURCHASE AGREEMENTS	
IE314	606-10-55-400
Example 62—Repurchase Agreements	
IE315	606-10-55-401
IE316	606-10-55-402
IE317	606-10-55-403
IE318	606-10-55-404
IE319	606-10-55-405
IE320	606-10-55-406
IE321	606-10-55-407

BILL-AND-HOLD ARRANGEMENTS	
IE322	606-10-55-408
Example 63—Bill-and-Hold Arrangement	
IE323	606-10-55-409
IE324	606-10-55-410
IE325	606-10-55-411
IE326	606-10-55-412
IE327	606-10-55-413

Appendix B

Amendments to the Basis for Conclusions on other Standards

The amendments in this appendix to the Basis for Conclusions on other Standards are necessary in order to ensure consistency with IFRS 15 and the related amendments to other Standards.

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The amendments contained in this appendix when IFRS 15 was issued in 2014 have been incorporated into the Basis for Conclusions on the relevant Standards included in this volume.

