

**Mr Hans Hoogervorst  
International Accounting  
Standards Board  
30 Cannon Street  
London  
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United Kingdom**

**Ref: The IASB's Exposure Draft *Clarifications to IFRS 15***

Dear Mr Hoogervorst,

The European Securities and Markets Authority (ESMA) thanks you for the opportunity to contribute to the IASB's due process regarding the Exposure Draft (ED) *Clarifications to IFRS 15 Revenue from Contracts with Customers*. We are pleased to provide you with the following comments with the aim of improving the enforceability of IFRSs and the transparency and decision usefulness of financial statements.

ESMA agrees with the proposed clarifications to IFRS 15 in response to issues arising from the discussions of the Transition Resource Group for Revenue Recognition (TRG). However, ESMA regrets that the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) were not able to maintain convergence between the requirements of IFRS 15 and Topic 606 of the Codification and urges the two boards to maintain their efforts to keep the standards as convergent as possible.

ESMA agrees that the IASB identified the right issues that require clarification from the TRG discussions and that no further clarification on the issues for which amendments are proposed by the FASB is required at this stage. We also support the IASB's decision to include a discussion in the Basis for Conclusions to the ED of the potential impacts on convergence for each of the issues where either the IASB or the FASB have decided to propose different amendments to their respective standards. However, ESMA notes that the difference in the amendments proposed by the IASB and FASB might lead to different outcomes even in circumstances when that was not intended by the Boards.

Furthermore, ESMA encourages the IASB to discuss emerging issues together with the FASB in order to retain the current level of convergence, when possible. Should divergence arise, we recommend the IASB to clearly identify and communicate any such differences between IFRS 15 and Topic 606 and update the comparison in Appendix A to the Basis for Conclusions of IFRS 15 as the Boards' proposals are finalised or new differences emerge.

ESMA continues to believe that the joint TRG should be maintained until the date of mandatory adoption of IFRS 15. While we are of the view that with these amendments the



standard-setting activity of the IASB should be finished, the TRG should continue to assist market participants in implementing the new standard.

Regarding any further standard-setting process related to IFRS 15, unless a major flaw of the standard is identified, any remaining minor issues to be identified by the implementation process could be addressed by referring the issue for consideration to the IFRS Interpretation Committee or to the post-implementation review. Indeed, ESMA believes that, at this stage, before the date of mandatory application of IFRS 15, the IASB should only clarify those issues that are strictly necessary for a proper understanding of the standard, in order to ease the implementation and to foster consistent application.

ESMA encourages the IASB to find a way to make easily accessible to all IFRS constituents, the analysis of the issues that were referred to the IASB by the TRG and for which no clarification was provided. This might be even more relevant after the period of first time application of the Standard when the TRG will be no longer active. In this respect, ESMA is of the view that such an analysis could be published as educational material in the framework of the IASB Educational Initiative.

Our detailed comments on the ED are set out in the Appendix I to this letter. Please do not hesitate to contact us should you wish to discuss all or any of the issues we have raised.

Yours sincerely,

A handwritten signature in blue ink, appearing to be 'S/M' with a flourish.

Steven Maijor

cc: Russel G. Golden, Chairman, Financial Accounting Standards Board

## Appendix I – ESMA’s detailed answers to the questions in the ED

### Question 1 – Identifying performance obligations

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

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

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

#### Identifying performance obligations

1. ESMA agrees with the proposed amendments to the Illustrative Examples accompanying IFRS 15 related to identifying performance obligations. ESMA agrees with the approach proposed by the IASB to illustrate the application of the existing principle rather than broader clarification proposed by the FASB.
2. While ESMA understands that the IASB expects that the modifications made to the standard itself by the FASB will not change the analysis and that the principles remains the same, ESMA encourages the IASB to explain in the Basis for Conclusions how it reached this conclusion.
3. We have some concerns on the Illustrative example 10 as the conclusions reached in the example are not explicitly linked to any of the principles described in the Standard. As it is difficult to understand the rationale followed in this example, ESMA encourages the IASB either to delete this example or to provide more explanations on the analysis made and rationale used. As this example is also in the FASB ED, ESMA expects the IASB and the FASB to reach the same conclusions.

#### Identifying immaterial goods or services

4. ESMA believes that additional amendments relating to promised goods or services that are immaterial in the context of a contract proposed by the FASB are not necessary. ESMA believes that the concept of materiality is pervasive in financial reporting and should not be specifically defined for the purposes of identification of a performance obligation in IFRS 15. On the contrary, doing so might create the impression that for

these type of transactions a different materiality threshold is applicable, which cannot be true.

*Shipping and handling activities*

5. ESMA would disagree with the introduction of an accounting policy election relating to shipping and handling activities as such accounting policy choice would decrease comparability of financial statements. ESMA agrees with the IASB that such an accounting policy choice would override the principle in paragraph 22 of IFRS 15 that requires an entity to assess goods or services promised in a contract with a customer in order to identify a performance obligation.
6. While ESMA welcomes the proposed wording in the Basis for Conclusions (in particular, paragraph BC24) because it states that the practical expedient would override IFRS 15 principles, we are of the view that a more explicit wording might be required to prevent IFRS preparers to apply US GAAP by analogy.

**Question 2 – Principal versus agent considerations**

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

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

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

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

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

7. ESMA is of the view that the proposed amendments make the wording of the standard more consistent with the underlying principle. Consequently, ESMA agrees with the proposed clarifications and with the proposed new illustrative examples accompanying IFRS 15. ESMA also welcomes the full convergence topic between the proposals of the IASB and FASB and encourage the Boards to finalise these proposals jointly.

8. ESMA agrees that the existing guidance in paragraphs B34 and B35 of IFRS 15 may have created confusion. In particular, certain implementation issues might have arisen because there was no clear link between the indicators in paragraph B37 and the control principle. Therefore, ESMA welcomes the proposed amendments which clarify the standard and make an explicit link between the control principle in paragraph B35A and the indicators in paragraph B37.
9. Principal versus agent considerations currently pose major challenge in the accounting for many contracts. While the guidance in paragraph B37 addresses certain issues, ESMA points out that some sources of possible diversity remain. For instance, regarding the proposed assessment of credit risk in paragraph B37(d) is inconclusive as it states that (1) the exposure to credit risk for the amount receivable from the customer in exchange for the specified good or service is an indicator for being a principal but at the same time that (2) an agent might choose to accept credit risk as part of its overall service of arranging for the provision of the specified good or service.

### **Question 3 – Licencing**

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

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

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

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

10. ESMA supports the proposed amendments to IFRS 15 regarding licensing.
11. ESMA agrees with the proposed clarification that enables to assess the nature of the entity’s promise and better articulates circumstances when entity’s activities significantly

affect the intellectual property. ESMA is of the view that this proposed clarification will contribute to consistent application of the guidance in this area.

12. Furthermore, ESMA agrees with the proposed clarifications in paragraphs B63A and B63B of IFRS 15 regarding sales-based and usage-based royalties promised in exchange for licenses of intellectual property ('royalties constraint'). ESMA welcomes the additional guidance on the application of the royalties constraint as well as moment of the recognition of revenue.
13. We particularly welcome paragraph BC70 in the Basis for Conclusions that explicitly refers to situations where the approaches of the IASB and the FASB may lead to different outcomes as a consequence of different decisions on this issue. In our view it will mitigate the risk of IFRS constituents applying US GAAP by analogy.
14. ESMA agrees with the IASB that the more extensive amendments to the licencing guidance proposed by the FASB are not necessary. In particular, ESMA agrees that clarification about the effect of contractual restrictions in licencing agreements on the identification of the promised goods or services in the contract is not needed as the underlying principle is clear.
15. However, while ESMA agrees with what is stated in paragraph BC81 of the ED that the IASB's analysis is based only on the application of existing principles in the standard, we suggest that the IASB includes an analysis of additional fact patters in the Illustrative Examples to IFRS 15 in order to demonstrate the application of these principles. Adding such examples will facilitate consistent application of IFRS 15 in this area.

#### **Question 4 – Practical expedients to transition**

*The IASB is proposing the following two additional practical expedients on transition:*

*(a) to permit an entity to use hindsight in (i) identifying the satisfied and unsatisfied performance obligations in a contract that has been modified before the beginning of the earliest period presented; and (ii) determining the transaction price.*

*(b) to permit an entity electing to use the full retrospective method not to apply IFRS 15 retrospectively to completed contracts (as defined in paragraph C2) at the beginning of the earliest period presented.*

*The reasons for the IASB's decisions are explained in paragraphs BC109–BC115. The FASB is also expected to propose a practical expedient on transition for modified contracts.*

*Do you agree with the proposed amendments to the transition requirements of IFRS 15? Why or why not? If not, what alternative, if any, would you propose and why?*

16. ESMA acknowledges that the application of the contract modification guidance can be challenging upon transition for entities with many contract modifications before the date

of initial application. Consequently, ESMA agrees with the additional practical expedient on transition to IFRS 15 permitting an entity to use hindsight in identifying the satisfied and unsatisfied performance obligations in a contract that has been modified before the beginning of the earliest period presented and in determining the transaction price.

17. Furthermore, ESMA agrees that an entity does not need to restate contracts that are completed at the beginning of the earliest period presented.
18. While these amendments could affect the comparability of financial information under the full retrospective method, they do not imply a significant departure from the revenue model and a possible decrease in comparability is outweighed by facilitating and reducing the costs of implementing IFRS 15.
19. However, we are concerned about the different possible interpretations of the term 'completed contracts' in IFRS 15 as it was evidenced in the July 2015 TRG meeting, where divergent views were expressed by the TRG members. Therefore, ESMA recommends that the IASB considers during its re-deliberations of this ED additional discussions that might take place at the TRG on this topic. If the notion of 'completed contracts' and its subsequent accounting are not sufficiently clear, it may lead to development of divergence in practice.
20. In this respect, if the IASB concludes that there could be unrecognised revenue on completed contracts upon transition to IFRS 15, ESMA encourages the IASB to explicitly address its accounting treatment as part of these Clarifications to IFRS 15.

### **Question 5 – Other topics**

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

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

21. ESMA is of the view that no amendments to IFRS 15 are required with respect to these issues. ESMA welcomes the IASB's decision in the ED to include a discussion in the Basis for Conclusions of the potential impacts on convergence for each of the issues where either the IASB or the FASB has decided to propose different amendments to their respective standards. However, should additional divergence arise in the future, we recommend the IASB to clearly identify and communicate any such differences between IFRS 15 and Topic 606 and update the comparison in Appendix A to the Basis for

Conclusions of IFRS 15 as the Board's proposals are finalised and new differences emerge.

22. ESMA encourages the IASB to find a way how the analysis of the TRG and the IASB conclusions on these topics can be made more easily accessible to all IFRS constituents. This might be even more relevant after the period of first-time application of the Standard when the TRG will be no longer active. In this respect, ESMA is of the view that this analysis and/or conclusions of the TRG on selected issues could be published as educational material in the framework of the IASB Educational Initiative.

#### Collectability

23. ESMA agrees with the IASB's decision not to clarify this issue for the reasons explained in the Basis for Conclusions of the ED. However, ESMA points out that the FASB proposals clarifying how an entity should assess collectability in Step 1 of the revenue recognition model are not yet available. Consequently, when the ED becomes available before finalisation of the FASB's amendments, ESMA encourages the IASB to update the Basis for Conclusion (paragraph BC 93 of the ED) for the actual proposals of the FASB.

#### Measuring non-cash consideration

24. ESMA agrees with the IASB's decision not to provide guidance either on the measurement date of the non-cash consideration or on when to apply the constraint on variable consideration in situations where the fair value of the non-cash consideration varies because of the form of the consideration and for reasons other than the form of the consideration.
25. ESMA acknowledges that the existing IFRS literature does not include specific requirements on the measurement date for non-cash consideration as well as the IASB's arguments in paragraph BC 102 of the ED that discussions with stakeholders highlighted that practical effect of different measurement dates would arise only in limited circumstances. Furthermore, ESMA notes the IFRS IC plans to publish a Draft IFRIC Interpretation of IAS 21 *The Effects of Changes in Foreign Exchange Rates* that will clarify the accounting for transactions in foreign currency that contain a payment or receipt of advance consideration. Due to the interactions with that issue, we agree with the IASB's decision stated in paragraph BC 100 of the ED to consider, if needed, the measurement date of the non-cash consideration more comprehensively in a separate project.

#### Presentation of sales taxes

26. ESMA would disagree with the introduction of an accounting policy election relating to presentation of sales taxes either on a gross or on a net basis as such accounting policy choice would decrease comparability of IFRS financial statements and would create an exception to the revenue recognition model that does not reflect the economics of the arrangement in cases for which a sales tax is a tax on the entity rather than a tax collected by the entity from the customer on behalf of the tax authority.