iGAAP in Focus

Financial reporting

IASB seeks views on the post-implementation review of IFRS 15

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This *iGAAP in Focus* outlines the Request for Information (RFI) *Post-implementation Review of IFRS 15 Revenue from Contracts with Customers*, published by the International Accounting Standards Board (IASB) in June 2023.

- The IASB launched a call for stakeholders' feedback on its post-implementation review of IFRS 15 *Revenue from Contracts with Customers*
- In particular, the IASB is asking questions on the following areas:
  - Overall assessment of IFRS 15
  - Identifying performance obligations in a contract
  - Determining the transaction price
  - Determining when to recognise revenue
  - Principal versus agent considerations
  - Licensing
  - Disclosure requirements
  - Transition requirements
  - Applying IFRS 15 with other IFRS Accounting Standards
  - Convergence with Topic 606 *Revenue from Contracts with Customers*
  - Other matters
- The RFI is open for comments until 27 October 2023

Background

IFRS 15 *Revenue from Contracts with Customers* became effective for annual periods beginning on or after 1 January 2018. IFRS 15 was developed jointly with the US Financial Accounting Standards Board (FASB) and created a comprehensive and robust framework for the recognition, measurement and disclosure of revenue arising from contracts with customers.

In September 2022, the IASB started its post-implementation review (PIR) of IFRS 15. The IASB now published an RFI seeking information on the matters identified in the first phase of the PIR and any other information relevant to the PIR.

Questions for respondents

Overall assessment of IFRS 15

IFRS 15 establishes the principles that an entity applies to report useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer. To meet the objective, IFRS 15:

- Establishes a core principle for revenue recognition, which is that an entity recognises revenue to depict the transfer of promised goods or services to the customer in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services
- Relies on a five-step model to support the core principle. The five steps an entity applies in recognising revenue are:
  - Step 1—identify the contract(s) with a customer
  - Step 2—identify the performance obligations in the contract
  - Step 3—determine the transaction price
  - Step 4—allocate the transaction price to the performance obligations in the contract
  - Step 5—recognise revenue when (or as) the entity satisfies a performance obligation

> **Observation**
>
> Stakeholder feedback suggested that IFRS 15 has achieved its objective and is working well, although some stakeholders still find applying aspects of the requirements challenging. Stakeholders generally see the five-step revenue recognition model as helpful—in particular, as a robust basis for analysing complex transactions.
>
> A few stakeholders suggested that the Standard might be too complex to apply for smaller entities and for entities in emerging economies. In addition, some stakeholders said that entities need to use significant judgement in applying the requirements in IFRS 15 to complex fact patterns, which might lead to inconsistent outcomes among entities. On the other hand, stakeholders also expressed concern about the IASB making fundamental changes to IFRS 15 that would result in disruption.

The RFI asks whether IFRS 15 achieved its objective. Respondents are asked to explain whether the core principle and the supporting five-step revenue recognition model provide a clear and suitable basis for revenue accounting decisions that result in useful information about an entity's revenue from contracts with customers. If not, respondents are asked to explain the fundamental questions (fatal flaws) about the clarity and suitability of the core principle or the five-step revenue recognition model.

The RFI also asks for any feedback on the understandability and accessibility of IFRS 15 that the IASB could consider in developing future Standards or in assessing whether, and if so how, the IASB could improve the understandability of IFRS 15 without changing its requirements or causing significant cost and disruption to entities already applying the Standard—for example, by providing education materials or flowcharts explaining the links between the requirements.

The IASB would like to know the ongoing costs and benefits of applying the requirements in IFRS 15 and how significant they are. If the ongoing costs of applying IFRS 15 are significantly greater than expected or the benefits of the resulting information to users of financial statements are significantly lower than expected, respondents are asked to explain why they hold this view.

The IASB is interested whether there is diversity in application of the Standard in respect of many of the areas analysed in the RFI. For these areas, respondents are asked to explain and provide supporting evidence about how pervasive the diversity is and what causes it. Respondents should also explain how the diversity affects financial statements and the usefulness of the resulting information to users of financial statements.

Additionally, the RFI asks for suggestions for resolving the matters respondents have identified.

Identifying performance obligations in a contract

IFRS 15 requires an entity to identify performance obligations in its contracts with customers. A performance obligation is defined as a promise in a contract with a customer to transfer to the customer either a good or service (or a bundle of goods or services) that is distinct, or a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.

Observation

Stakeholder feedback suggested that it is sometimes challenging to identify goods or services promised in a contract and to determine whether those goods or services are distinct. In particular, for:

- Arrangements involving internally developed products or digital products, for example, web-based software applications
- Contract modifications
- Licensing arrangements
- Arrangements in which an entity uses its judgement to determine whether it is acting as an agent or a principal

The RFI asks whether IFRS 15 provides a clear and sufficient basis to identify performance obligations in a contract. Respondents are asked to describe fact patterns in which the requirements:

- Are unclear or are applied inconsistently
- Lead to outcomes that do not reflect the underlying economic substance of the contract
- Lead to significant ongoing costs

Determining the transaction price

IFRS 15 defines the transaction price as the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties (for example, some sales taxes). The Standard also provides specific requirements for determining the transaction price if consideration includes a variable amount, a significant financing component or consideration payable to the customer.

Observation

Some stakeholders indicated that they are unsure as to how to account for incentives offered in three-way arrangements when a party acting as an agent pays a marketing incentive to end customers—for example, when a digital platform entity offers incentives to end customers who buy goods or services such as food delivery or taxi services through the platform. The feedback suggests that some entities treat these incentives as payments to customers, i.e. as a reduction of revenue. Others treat these incentives as marketing expenses. This diversity in application might reduce the usefulness of revenue information to users of financial statements.

Some stakeholders also indicated there was a lack of clarity on how to account for consideration payable to a customer if it exceeds the amount of consideration expected to be received from the customer—for example, when an entity wishing to enter a highly competitive market offers large incentives to attract customers. Initial feedback suggested that some entities present the amount of consideration payable exceeding the consideration receivable as 'negative' revenue. Other entities reclassify that excess as an expense.

The RFI asks whether IFRS 15 provides a clear and sufficient basis to determine the transaction price in a contract—in particular, in relation to accounting for consideration payable to a customer. Respondents are asked to describe fact patterns in which the requirements on how to account for incentives paid by an agent to the end customer or for negative net consideration from a contract are unclear or are applied inconsistently.

Determining when to recognise revenue

IFRS 15 requires an entity to recognise revenue when (or as) the entity transfers goods or services to a customer, which is when (or as) the customer obtains control of that good or service.

IFRS 15 includes criteria for determining whether control is transferred, and hence revenue recognised, over time.

Observation

Stakeholder feedback suggested that many entities have largely overcome initial challenges related to determining whether to recognise revenue over time or at a point in time. However, in some cases, for example, in the software development, gaming and construction industries, some challenges remain. Some stakeholders said that assessments based on the third criterion (which results in revenue being recognised over time when the entity's 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) can be especially challenging, notably in relation to the enforceability of an entity's right to payment.

The RFI asks whether IFRS 15 provides a clear and sufficient basis to determine when to recognise revenue. Respondents are asked to describe fact patterns in which the requirements are unclear or are applied inconsistently—in particular, in relation to the criteria for recognising revenue over time.

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 a principal or an agent based on the nature of its promise and on whether it controls the good or service before it is transferred to the customer. To help an entity assess whether it controls a specified good or service before it is transferred to a customer, IFRS 15 provides a non-exhaustive list of indicators of control.

Observation

Stakeholder feedback suggested that entities sometimes find applying the concept of control alongside the related indicators challenging. Some stakeholders suggested that the concept of control is not well understood—especially in relation to services. The IASB also heard that some entities assess whether they are a principal or an agent based solely on the indicators and overlook the concept of control. Some stakeholders also said that entities sometimes have difficulties to apply the indicators if those indicators point to different conclusions or if an arrangement involves more than three parties.

The RFI asks whether IFRS 15 provides a clear and sufficient basis to determine whether an entity is a principal or an agent. Respondents are asked to describe fact patterns in which the requirements are unclear or are applied inconsistently—in particular, in relation to the concept of control and related indicators.

Licensing

For contracts that grant licences of intellectual property (IP) to customers, IFRS 15 requires an entity:

- To determine whether the promise to grant a licence is distinct from other goods or services promised in the contract
- To consider the nature of the licence to determine whether the licence transfers to a customer either at a point in time or over time

Observation

Stakeholder feedback suggested that sometimes entities find the requirements for accounting for licensing arrangements unclear or apply them inconsistently. For example, stakeholders asked the IASB to clarify how:

- To determine whether an arrangement is a licensing arrangement if the contract refers to licensing but is in substance similar to a sale of IP or service provision
- To identify performance obligations in arrangements that include an obligation to provide goods or services as well as a licence
- To account for licence renewals. Stakeholders commented that some entities recognise revenue when the renewal period starts, and others recognise it when the renewal is agreed. Some stakeholders noted that the FASB has amended Topic 606 *Revenue from Contracts with Customers* to clarify that an entity is not permitted to recognise revenue from a licence renewal until the beginning of the renewal period

The RFI asks whether IFRS 15 provides a clear and sufficient basis for accounting for contracts involving licences. Respondents are asked to describe fact patterns in which the requirements are unclear or are applied inconsistently—in particular, in relation to the matters raised by stakeholders.

Disclosure requirements

In developing IFRS 15, the IASB sought to improve on the disclosure requirements in previous Standards to enable entities to provide more useful information about the nature, amount, timing and uncertainty of revenue.

IFRS 15 requires an entity to disclose information about:

- Revenue recognised from contracts with customers
- Any impairment losses recognised on receivables or contract assets arising from contracts with customers
- Contract balances
- Performance obligations
- Significant judgements and changes in judgements made in applying the requirements
- Assets recognised from the costs to obtain or fulfil a contract with a customer
- Practical expedients used

Observation
Stakeholder feedback on the disclosure requirements was generally positive. Some users of financial statements, regulators and accounting firms said they saw some improvement in the usefulness of information entities disclosed about revenue after IFRS 15 was implemented.

Stakeholders' main concerns about the disclosure requirements related to the costs of meeting some disclosure requirements potentially exceeding the usefulness of the resulting information to users of financial statements and entities sometimes omitting the information required by IFRS 15. Some stakeholders suggested this issue might be caused by a lack of specificity in the disclosure requirements.

The RFI asks whether the disclosure requirements in IFRS 15 result in entities providing useful information to users of financial statements. Respondents are asked to identify any disclosures that are particularly useful to users of financial statements and explain why. Respondents should also identify any disclosures that do not provide useful information and explain why the information is not useful.

The RFI also asks whether any disclosure requirements in IFRS 15 give rise to significant ongoing costs. Respondents should explain why meeting the requirements is costly and whether the costs are likely to remain high over the long term.

In addition, respondents are asked whether they observed significant variation in the quality of disclosed revenue information. If so, they should explain what causes such variation and what steps, if any, could the IASB take to improve the quality of the information provided.

Transition requirements
The IASB allowed an entity applying IFRS 15 for the first time a choice between two transition methods, namely:

- Applying the Standard retrospectively to each prior reporting period presented, subject to practical expedients allowed by IFRS 15 (retrospective method)
- Applying the Standard retrospectively with the cumulative effect of initially applying IFRS 15 recognised at the date of initial application (modified retrospective method)

In addition, the IASB introduced practical expedients to reduce the cost and burden of transition for preparers of financial statements.

The RFI asks whether the transition requirements work as the IASB intended. Respondents are asked to explain whether entities applied the modified retrospective method or the practical expedients and why, and whether the transition requirements in IFRS 15 achieved an appropriate balance between reducing costs for preparers of financial statements and providing useful information to users of financial statements.

Applying IFRS 15 with other IFRS Accounting Standards
IFRS 15 requires an entity to apply the requirements in the Standard to all contracts with customers, except:

- Lease contracts within the scope of IFRS 16 *Leases*
- Contracts within the scope of IFRS 17 *Insurance Contracts* (with some limited exceptions)
- Financial instruments and other contractual rights or obligations within the scope of IFRS 9 *Financial Instruments,* IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements,* IAS 27 *Separate Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures*
- Non-monetary exchanges between entities in the same line of business to facilitate sales to customers or potential customers

Observation

Stakeholders raised the following concerns with regard to the application of IFRS 15 with other IFRS Accounting Standards:

- The difference between the measurement principles in IFRS 3 *Business Combinations* (based on fair value) and those in IFRS 15 (based on the transaction price) can create difficulties for entities when measuring contract assets and contract liabilities acquired as part of a business combination
- Some stakeholders are unsure whether to apply the requirements in IFRS 15 or those in IFRS 9, in particular when:
  - An entity accepts lower consideration from a customer whose financial position has deteriorated over the course of their relationship
  - IFRS 15 gives rise to liabilities but does not include guidance on how to account for them
- Some entities find accounting for contracts that include a service component and a lease component difficult due to differences between the requirements in IFRS 15 and IFRS 16
- It is unclear how to account for transactions in which an entity—as part of its ordinary activities—sells an asset by selling an equity interest in a single-asset entity that is a subsidiary (a so-called 'corporate wrapper')

The RFI asks whether it is clear how to apply the requirements in IFRS 15 with the requirements in other IFRS Accounting Standards. Respondents are asked to describe and provide supporting evidence about fact patterns in which this is not the case, how pervasive the fact patterns are, what causes the ambiguity and how that ambiguity affects entities' financial statements and the usefulness of the resulting information to users of financial statements. The IASB is particularly interested in respondents' experience with the concerns raised by stakeholders

Convergence with Topic 606 *Revenue from Contracts with Customers*

IFRS 15 was developed jointly with the FASB. In May 2014, the IASB issued IFRS 15 and the FASB issued Topic 606. When issued, the requirements in IFRS 15 and Topic 606 were substantially converged, except for some minor differences.

In deciding whether to take action on its PIR findings, the IASB will need to consider how any actions will affect convergence between IFRS 15 and Topic 606. As part of this consideration, the IASB is seeking respondents' views on how important retaining the current level of convergence between IFRS 15 and Topic 606 is.

Other matters

Respondents are asked to share feedback on other matters relevant to the PIR, such as whether:

- There are fundamental questions (fatal flaws) about the clarity and suitability of the core objective or principles in IFRS 15
- The benefits to users of financial statements of the information arising from applying IFRS 15 requirements are significantly lower than expected
- The costs of applying IFRS 15 requirements and auditing and enforcing their application are significantly greater than expected

The RFI asks to explain why those matters should be considered in the context of the PIR and the pervasiveness of any matter raised. Respondents are asked to provide examples and supporting evidence.

Comment period and next steps

The RFI is open for comments until 27 October 2023.

After the comment period ends, the IASB will consider comments from the public consultation along with information gathered from any additional analysis and other consultative activities. The IASB will then publish a report and feedback statement summarising its findings and, if any, next steps. The next steps may include providing educational materials or considering possible standard-setting.

Further information

If you have any questions about the RFI, please speak to your usual Deloitte contact or get in touch with a contact identified in this *iGAAP in Focus.*

The Deloitte Accounting Research Tool (DART) is a comprehensive online library of accounting and financial disclosures literature. **iGAAP on DART** allows access to the full IFRS Standards, linking to and from:

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