Dr Andreas Barckow 25 October 2023

Chair of the International Accounting Standards Board
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Submitted to: www.ifrs.org

Dear Andreas

Request for information on the Post-implementation review of IFRS 15: *Revenue from Contracts with Customers ('the RFI')*

Thank you for the opportunity to comment on the RFI.

IFRS 15 is working well in New Zealand for the majority of contracts, with some exceptions for more complex or bespoke contracts. Principal versus agent considerations remain an issue and we have the following recommendations in this area:

a) Give greater prominence to the assessment of transfer of control as being the primary assessment in determining whether a reporting entity is a principal or agent.
b) Make substantive revisions to the indicators with the objective of clearly linking each indicator to the concept of control.
c) Add new, up-to-date illustrative examples.

Our recommendations and responses to the specific questions are provided in the Appendix to this letter. If you have any queries or require clarification of any matters in this letter, please contact Leana van Heerden (leana.vanheerden@xrb.govt.nz) or me.

Yours sincerely

Carolyn Cordery
Chair – New Zealand Accounting Standards Board

Appendix

Question 1:
Overall assessment of IFRS 15

(a) In your view, has IFRS 15 achieved its objective? Why or why not?
Please 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, please explain what you think are the fundamental questions (fatal flaws) about the clarity and suitability of the core principle or the five-step revenue recognition model.

(b) Do you have any feedback on the understandability and accessibility of IFRS 15 that the IASB could consider:
(i) in developing future Standards; or
(ii) in assessing whether, and if so how, it 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?

(c) What are the ongoing costs and benefits of applying the requirements in IFRS 15 and how significant are they?
If, in your view, 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, please explain why you hold this view.

These questions aim to help the IASB understand respondents' overall views and experiences relating to IFRS 15. Sections 2–9 seek more detailed information on specific requirements.

Response to Question 1

Question 1a - In your view has IFRS 15 achieved its objective?

1. IFRS 15 is working well for the majority of contracts, with some exceptions for more complex or bespoke contracts. The introduction of the five-step revenue recognition model brought greater rigour to entities' assessments of their revenue contracts and users have told us that the disclosures usually strike the right balance. On this basis, in our view IFRS 15 has achieved its objective.

Question 1b and 1c

- *Do you have feedback on the understandability and accessibility of IFRS 15 that the IASB could consider?*

- *What are the ongoing costs and benefits of applying the requirements in IFRS 15 and how significant are they?*

2. Flowcharts in areas with multiple decision points would help to improve the understandability and accessibility of the requirements. Additionally, illustrative examples that are relevant to today's business environment would assist entities with application. Consideration of IFRS 15 related IFRIC Agenda Decisions may help to identify relevant examples.

3. Some IFRS 15 requirements, such as when dealing with significant financing components and variable consideration calculations, may not be supported by finance systems. This necessitates manual calculations using excel spreadsheets and the use of manual journal entries which is resource intensive and prone to error. The IASB should reflect on whether they were aware of these implications during deliberations on the Standard and embed any learnings into future standard setting. We do not think amendments to IFRS 15 on these points would be beneficial at this time as stakeholders have little appetite for disruptive changes.

Question 2

Identifying performance obligations in a contract

(a) Does IFRS 15 provide a clear and sufficient basis to identify performance obligations in a contract? If not, why not?

Please describe fact patterns in which the requirements:

(i) are unclear or are applied inconsistently;

(ii) lead to outcomes that in your view do not reflect the underlying economic substance of the contract; or

(iii) lead to significant ongoing costs.

If diversity in application exists, please explain and provide supporting evidence about how pervasive the diversity is and explain what causes it. Please also explain how the diversity affects entities' financial statements and the usefulness of the resulting information to users of financial statements.

(b) Do you have any suggestions for resolving the matters you have identified?

Response to Question 2

Question 2a – Does IFRS 15 provide a clear and sufficient basis to identify performance obligations in a contract?

4. IFRS 15 provides a clear and sufficient basis for identifying performance obligations in most cases. However, contracts with bespoke internally developed products, or arrangements involving multiple parties can require a high degree of judgement, particularly in determining whether promised goods or services are distinct in the context of the contract.

5. There are also challenges within the IT / ICT industry with respect to determining whether implementation type activities are a promised good or service that will be transferred to a customer. This is relevant to:

- Bespoke contracts that require some level of implementation with subsequent delivery.
- Managed services solutions where it is unclear whether certain set up activities are value-add to the customer, but it is possible to get another company to do the activity.

Question 2b – Do you have any suggestions for resolving the matters you have identified?

6. While the principles in IFRS 15 are clear, in certain circumstances entities may need to apply a high degree of judgement when determining whether an activity it will perform is a promised good or service that will be transferred to a customer, and whether the promised goods or services in a contract result in one or more performance obligations.

7. We recommend updating the illustrative examples in IFRS 15 so that they are more relevant to today's business environment to assist entities with application.

Question 5:

Principal versus agent considerations

(a) Does IFRS 15 provide a clear and sufficient basis to determine whether an entity is a principal or an agent? If not, why not?
Please 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 (see Spotlight 5).

If diversity in application exists, please explain and provide supporting evidence about how pervasive the diversity is and explain what causes it. Please also explain how the diversity affects entities' financial statements and the usefulness of the resulting information to users of financial statements.

(b) Do you have any suggestions for resolving the matters you have identified?

Response to Question 5

Question 5a – Does IFRS 15 provide a clear and sufficient basis to determine whether an entity is a principal or an agent?

8. Determining principal versus agent was a challenge prior to IFRS 15 and remains a challenge for many arrangements. This was the most frequently raised issue throughout our outreach in New Zealand and there is inconsistency in practice. Some of these transactions are inherently complex in terms of the number of parties involved and the rights and obligations of each of those parties. While judgment in this area cannot be eliminated, substantive changes are

needed to the indicators to better guide entities through principal versus agent assessments to reduce diversity in practice.

9. The focus on principal versus agent considerations is relatively recent. Therefore, it was not a key focus or objective when IFRS 15 was under development to substantially revise or improve principal versus agent accounting. Now that IFRS 15 is embedded and is working well for the majority of contracts, it is timely for the IASB to address this issue.

10. The IFRS 15 requirements focus on determining who controls each specified good or service before it is transferred to the customer. Despite this requirement in the Standard, and supporting wording in the Basis for Conclusions, it is clear that in practice many entities go straight to application of the indicators. This is further illustrated by the IFRS IC, May 2022 IFRS 15-related agenda decision (*Principal versus Agent: Software Reseller*) which gave little prominence to the assessment of control, instead focusing on the indicators.

11. This is a significant issue because there is a disconnect between how the indicators relate to the notion of control used throughout the rest of IFRS 15 (that is, how they relate to determining whether an entity has the ability to direct the use of, and obtain substantially all the remaining benefits from, a good or service). In addition, the indicators (for example inventory risk) in IFRS 15 are geared towards more traditional revenue contracts for goods, making it even more challenging for entities to apply the indicators in the context of services and intangibles.

Question 5b – Do you have any suggestions for resolving the matters you have identified?

12. The determination of principal versus agent will inherently involve judgement; it is the way this judgement is applied where greater consistency is required. To achieve this we recommend the following:

a) <u>Give greater prominence to the assessment of transfer of control as being the primary assessment in determining whether a reporting entity is a principal or agent.</u>
   - This could be achieved by moving BC385H to the Standard. BC385H states – "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."

b) <u>Make substantive revisions to the indicators</u>
   - The objective of revising the indicators would be to clearly link each indicator to the concept of control. For example, if we think about a **vendor** who is a manufacturer, an **entity** who is a reseller, and then an end **customer**, a clearly linked indicator would be:
     - o The entity has discretion in whether to consume the good or service for its own needs or transfer its right to a third party without needing permission from the vendor.
   - Understanding the business purpose and rationale for the contractual terms between the vendor and the entity should form a prominent part of the assessment. Indicators should be developed which help drive this thinking such as:

  - Does the vendor have on-going obligations to the entity <u>and if so why</u>? On-going obligations may include a return-to-vendor agreement, or a history of returning goods to the vendor after a customer returns the goods, and whether the vendor is the party that the customer will hold responsible for the acceptability of the product.
  - Is the entity's discretion on whether and how to consume or transfer the good or service limited <u>and if so why</u>? Limits to discretion may include pricing floors and ceilings set by the vendor, the vendor specifying customer orders to fulfil, the vendor having the right to take back delivered goods etc.
- Separate consideration of indicators for goods, versus services and intangibles may be required.
- Additional clarification should be added on how entities should weigh up the indicators when there is a mixed assessment. This should explain that it is not a matter of 'counting' the indicators, but rather through judgment placing greater weight on the indicators of most relevance to the arrangement, while also considering the arrangement holistically.

c) <u>Add new, up-to-date illustrative examples</u>

- The illustrative examples in IFRS 15 are widely used and entities have found them useful. However, given the illustrative examples were developed a number of years ago the usefulness is becoming more limited as new types of arrangements not covered by the examples have emerged and become more prevalent. It would be worthwhile adding new illustrative examples reflective of common arrangements in today's business environment, such as:
- **Online platforms** that connect sellers and buyers of digital products, such as e-books, music, or videos.
- **Cloud service providers** that offer cloud computing services, such as infrastructure as a service (IaaS), platform as a service (PaaS), or software as a service (SaaS), to end customers.
- **Managed service solutions** that offer one packaged solution to the customer but involves multiple deliveries that are outsourced.

Question 7:

Disclosure requirements

(a) Do the disclosure requirements in IFRS 15 result in entities providing useful information to users of financial statements? Why or why not?
Please identify any disclosures that are particularly useful to users of financial statements and explain why. Please also identify any disclosures that do not provide useful information and explain why the information is not useful.

(b) Do any disclosure requirements in IFRS 15 give rise to significant ongoing costs?
Please explain why meeting the requirements is costly and whether the costs are likely to remain high over the long term.

(c) **Have you observed significant variation in the quality of disclosed revenue information? If so, what in your view causes such variation and what steps, if any, could the IASB take to improve the quality of the information provided?**

Response to Question 7

Questions 7a and c

13. The increased revenue disclosures have provided benefit to users of financial statements. New Zealand users have indicated that usually revenue disclosures strike the right balance.

14. However, entities do not always re-evaluate their disclosures as their circumstances change which may result in missing, boilerplate, and/or immaterial disclosures. To help drive improvements in the quality of information the IASB could take an educative approach, reminding preparers of the importance to users of relevant, tailored, up-to-date disclosures.

Questions 3, 4, 6, 8, 9, 10 and 11

15. We have not commented on these questions.