

STAFF PAPER

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IFRS Interpretations Committee Meeting

Project	Revenue recognition in a real estate contract that includes the transfer of land (IFRS 15)		
Paper topic	Agenda decision to finalise		
CONTACT(S)	Craig Smith	csmith@ifrs.org	+44 (0)20 7246 6462

This paper has been prepared for discussion at a public meeting of the IFRS Interpretations Committee (Committee). Comments on the application of IFRS Standards do not purport to set out acceptable or unacceptable application of IFRS Standards—only the Committee or the International Accounting Standards Board (Board) can make such a determination. Decisions made by the Committee are reported in IFRIC® *Update*. The approval of a final Interpretation by the Board is reported in IASB® *Update*.

Introduction

1. The purpose of this paper is to provide the IFRS Interpretations Committee (Committee) with an analysis of the comments received on its tentative agenda decision published in November 2017 titled ‘Revenue recognition in a real estate contract that includes the transfer of land’.
2. The Committee received a submission about revenue recognition in a contract for the sale of land and a building to be constructed on the land. The land represents all of the area on which the building will be constructed, and the contract is for the entire building. Specifically, the submission asked (a) about the identification of performance obligations in the contract; and (b) for each performance obligation identified, whether the real estate developer (entity) recognises revenue over time or at a point in time.
3. In the tentative agenda decision, the Committee provided information about the application of paragraphs 22–30 and 35–37 of IFRS 15 *Revenue from Contracts with Customers* to real estate contracts more generally, as well as concluding on the application of those paragraphs to the fact pattern in the submission.
4. In identifying the number of performance obligations in a contract, the Committee noted that paragraphs BC105, BC116J and BC116K explain that the notion of ‘separately identifiable’ in paragraph 27(b) is influenced by the notion of separable

risks (ie whether the risk 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). An entity considers the level of integration, interrelation or interdependence among the promises to transfer goods or services. 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.

5. In the context of a contract for the sale of land and a building to be constructed on the land, the Committee observed that the promise to transfer the land would be separately identifiable from the promise to construct the building on that land if the entity concluded that (a) its performance in constructing the building would be the same regardless of whether the customer had purchased the land from it or another party; and (b) it would be able to fulfil its promise to construct the building even if the customer had purchased the land from another party, and would be able to fulfil its promise to transfer the land even if the customer had purchased the construction services from another developer.
6. In the fact pattern in the submission, the Committee observed that this would be the case and, thus, concluded that there are two performance obligations in the contract—ie a promise to transfer the land to the customer and a promise to construct the building on that land.
7. The Committee also concluded on the application of paragraph 35 to those performance obligations. The Committee observed that for the transfer of land, none of the criteria in paragraph 35 are met. Consequently, the entity recognises revenue for the transfer of the land to the customer at a point in time applying paragraph 38.
8. The Committee concluded that for the promise to construct the building, the customer controls the part-constructed building as it is being constructed. Accordingly, the criterion in paragraph 35(b) is met. The Committee noted the Board’s observation in paragraph BC129 that ‘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’.

9. The Committee concluded that the principles and requirements in IFRS 15 provide an adequate basis for an entity to recognise revenue in the fact pattern described in the submission. Consequently, the Committee decided not to add this matter to its standard-setting agenda.

Comment letter summary

10. As noted in Agenda Paper 2A, the Committee received eight comment letters on this tentative agenda decision. The comment letters are available on our [website](#).
11. Four of the eight respondents (Orange, the ASBJ, the ASCG, and Deloitte) say they agree, or do not disagree, with the Committee’s technical conclusion and analysis. Orange and Deloitte, nonetheless, suggest changes to the wording of the tentative agenda decision.
12. The ANAN says it agrees with the Committee’s decision not to add a project to its standard-setting agenda without commenting on the Committee’s technical analysis.
13. The ASBJ, the ASCG and the OIC each have concerns about the Committee providing answers for specific fact patterns—Agenda Paper 2B discusses these concerns.
14. The ANC and Mazars raise concerns about the Committee’s technical conclusion regarding the number of performance obligations in the fact pattern in the submission.
15. The remainder of this paper is organised as follows:
 - (a) Identification of performance obligations (paragraphs 17–37); and
 - (b) Other comments (paragraphs 33–35).
16. The paper has two appendices:
 - (a) Appendix A includes the proposed wording of the agenda decision; and

- (b) Appendix B includes a ‘clean’ version of the proposed agenda decision, with no mark-up.

Identification of performance obligations

Respondents comments

17. The ANC raises the following about the identification of performance obligations:
- (a) The tentative agenda decision mostly relies on the notion of a ‘transformative relationship’ (mentioned in the Basis for Conclusions on IFRS 15) to conclude that there are two performance obligations in the contract. The ANC suggests that the Committee consider how the requirements in IFRS 15 apply to the fact pattern before discussing concepts mentioned only in the Basis.
 - (b) The tentative agenda decision implies that the identification of the number of performance obligations depends on the number of parties with which an entity contracts. The ANC says contracting with different providers is not a determinative factor when identifying performance obligations, evidenced by cases A and B in Illustrative Example 10 to IFRS 15.
 - (c) The foundations of a building could be considered to transform the land. It says a functional relationship could be considered to be where work performed to date by the contractor could easily be removed or modified and would have no added value. It says in the fact pattern in the submission, if the contractor were to be replaced, a new contractor is unlikely to re-perform any work but if the work had to be modified or removed, then the cost of construction would be significantly modified. In its view, this could mean that there is a transformative relationship between the land and building.
18. Mazars agrees with the Committee’s decision to highlight paragraph BC116K in the tentative agenda decision but disagrees with the Committee’s technical conclusion. Mazars says the focus on the entity’s performance being different if the customer

were to acquire the land or building from a different entity focuses on the application of paragraph 27(a), rather than paragraph 27(b). In addition, it says the construction of the building transforms the land because, after construction, the land becomes ‘built land’. After construction of the building, the land will not be the same without significant deconstruction and restoration work.

19. Deloitte raises a concern about the wording in the tentative agenda decision [emphasis added]: ‘Is there a transformative relationship between the transfer of the land and the construction of the building? **In other words**, would the entity’s performance in constructing the building be any different had the customer already purchased the land from another party and vice versa?’. It says those words could be read as an interpretation of how the term ‘transformative relationship’ should be applied in all circumstances. It recommends replacing the phrase ‘in other words’ with ‘in this case’ or ‘for example’ to avoid any unwanted implications.

Staff analysis

20. For a good or service promised in a contract to be distinct, paragraph 27(b) requires that ‘the entity’s promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the promise to transfer the good or service is distinct within the context of the contract)’.
21. Paragraph 29 states that in assessing the criterion in paragraph 27(b), ‘the objective is to determine whether the nature of the promise, within the context of the contract, is to transfer each of those goods or services individually or, instead, to transfer a combined item or items to which the promised goods or services are inputs’.
- Paragraph 29 lists three factors that indicate that two or more promises are not separately identifiable:
- (a) The entity provides a significant service of integrating the goods or services with other goods or services promised in the contract into a bundle of goods or services that represent the combined output for which the customer has contracted.

- (b) One or more of the goods or services significantly modifies or customises, or are significantly modified or customised by, other goods or services promised in the contract.
- (c) The goods or services are highly interdependent or highly interrelated.

22. In our view, the Basis is helpful in explaining what the Board had in mind when it developed the criterion in paragraph 27(b) and the factors in paragraph 29. In particular, we note the following quotes from paragraphs BC105 and BC116K that were included in the tentative agenda decision:

...The notion of ‘separately identifiable’ is based on the notion of separable risks...(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)...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.

23. We think the explanations in these paragraphs help to explain ‘separately identifiable’ in paragraph 27(b) and also phrases such as ‘highly interdependent or highly interrelated’ in paragraph 29. We note that paragraph 27(b) requires the entity’s *promise* to transfer a good or service to the customer to be separately identifiable from other *promises* in the contract. The Basis notes that this means an entity considers the level of integration, interrelation or interdependence among the promises to transfer goods or services. The distinction between a transformative relationship and a functional relationship also helps to explain that the focus of the assessment is not on any physical dependency between the promised goods or services.

24. In the fact pattern in the submission, we think the promise to transfer the land is separately identifiable from the promise to construct the building. As noted in the

tentative agenda decision, there is a functional relationship between the land and the building. We think it is that functional relationship (in the context of the land and building, the physical dependency of the building on the land) on which some respondents have focussed in reaching a conclusion that there is a single performance obligation. However, as noted above, in assessing paragraph 27(b) it is important to focus on the integration and interdependence among the *promises* in the contract.

25. Illustrative Example 10A of IFRS 15 illustrates when an entity provides a significant integration service in a construction contract, and thus identifies a single performance obligation even though the construction involves many individual goods and services. Paragraph IE47 explains that the goods and services (such as site clearance, foundation, engineering, procurement, construction of the structure, etc.) are not separately identifiable applying paragraph 27(b) because the developer provides a significant service of integrating the good and services (the inputs) into a hospital (the combined output) for which the customer has contracted. In this respect, paragraph BC107 notes that ‘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’. In the fact pattern in the submission, we think the entity is providing a significant integration service in the context of the promise to construct the building (integrating the materials, labour, engineering, site clearance, etc. into the building (the combined output)). However we think there is little integration between the transfer of the land and the construction of the building, and thus the entity is not providing a significant service of integrating the land and the building as described in paragraph 29(a) and illustrated in Illustrative Example 10A.
26. In assessing whether a promise to transfer land is separately identifiable from a promise to construct a building on that land, we think the costs, or ease of removal, of work needed to prepare the land for construction is not a relevant consideration. If the contract included only the promise to construct the building on land already owned by the customer, then presumably the entity would need to dig into the land in preparing the land for construction. In our view, such work is an embedded part of the promise

to construct the building—in this respect, we note that in a contract to construct a hospital, Illustrative Example 10A of IFRS 15 lists ‘site clearance’ and ‘foundation’ as examples of the various promised goods and services that the entity integrates into the hospital (the combined output) for which the customer has contracted.

27. In considering the integration of the land and building, we note that land and a building are fundamentally different assets. This is evidenced by the fact that land generally has an unlimited economic life but buildings do not. The land will continue to exist in its existing form long after the end of the building’s economic life. Paragraph 58 of IAS 16 *Property, Plant and Equipment* requires an entity holding land and a building on the land to treat those as separate assets, even if they were acquired at the same time.

Wording of the agenda decision

28. Although we continue to agree with the Committee’s technical conclusion and analysis, we think improvements could be made to the wording of the agenda decision. We agree with respondents that the identification of performance obligations does not depend on the number of entities supplying services to a customer, and recommend removing from the tentative agenda decision the reference to obtaining the land or building from another party. Instead, we propose that the agenda decision refer to whether the work performed by the entity in constructing the building would be any different if it did not also transfer the land and vice versa.
29. We also agree with Deloitte’s suggestion to replace ‘in other words’ with ‘for example’, and have identified a number of other editorial changes to improve the clarity of the wording.
30. Finally, we also think almost all of the Committee’s analysis regarding the identification of performance obligations could be applied more generally to any contract that involves the transfer of land and of a building on that land—ie the analysis does not depend on the particular facts in the fact pattern in the submission. For this reason, we suggest moving that analysis to the general section of the agenda decision.

31. If the Committee agrees with this recommendation, then we recommend that the Committee would not formally conclude on the number of performance obligations in the contract. Instead, when applying paragraph 35 to the fact pattern in the submission we would include an assumption that the entity has identified two performance obligations in the contract. We think this aligns with the approach to responding to questions outlined in Agenda Paper 2B because, in our view, the information provided would achieve the objective of supporting a common understanding of the requirements.
32. Appendix A to this paper outlines these recommendations regarding the wording of the agenda decision.

Other comments

Respondent comments

33. Orange and Mazars suggest that the Committee not only address the application of paragraph 35(b) to the construction of the building assuming there are two performance obligations in the contract, but also assuming there is a single performance obligation. In particular, Mazars mentions it would be helpful to understand the consequences of the transfer of legal ownership of the land.
34. Orange also suggests that the agenda decision state that the customer is a housing association and is purchasing the entire building. Orange says this is important to clarify that the entity bears no risk from commercialising the individual units in that building. Orange also suggests that the agenda decision clarify that once the land is sold, the entity bears no further risk relating to that land (eg geological or environment risks).

Staff analysis

35. As discussed earlier in the paper, we continue to think there are two performance obligations in the fact pattern in the submission. If the Committee agrees with our analysis, then we recommend that the Committee does not analyse the fact pattern

assuming there is a single performance obligation in the contract. This is because we fear it would be misleading if we were to assume a single performance obligation in relation to a fact pattern for which we think there are two performance obligations applying paragraphs 22-30. We recommend no change in this respect in the agenda decision.

36. We agree with the suggestion to clarify that the contract is for the construction of an entire building—this is an important distinction between the fact pattern discussed in this paper and the fact patterns discussed in Agenda Papers 2C and 2E. We do not however suggest mentioning that the customer is a housing association. To do so might imply that there is some significance to this fact in the context of applying the relevant requirements in IFRS 15, which is not the case.

Staff recommendation

37. Based on our analysis in paragraphs 20–32 and 35–36 of this paper, we recommend confirming the tentative agenda decision published in [IFRIC Update](#) in November 2017.
38. Appendix A to this paper outlines the proposed wording of the agenda decision, showing the recommended changes as a mark-up to the tentative agenda decision. Appendix B to this paper includes a ‘clean’ version of the proposed agenda decision, without any mark-up.

Questions for the Committee
<p>1. Does the Committee agree with our recommendation to finalise the agenda decision?</p> <p>2. Does the Committee have any comments on the proposed wording of the agenda decision outlined in Appendix A to this paper?</p>

Appendix A—Proposed wording for agenda decision

- A1. We propose the following wording for the final agenda decision (new text is underlined and deleted text is struck through). Text moved within the agenda decision is not shown in mark-up.

Revenue Recognition in a Real Estate Contract that Includes the Transfer of Land (IFRS 15 *Revenue from Contracts with Customers*)

The Committee received a request about revenue recognition in a contract for the sale of land and a building to be constructed on the land. The land represents all of the area on which the building will be constructed and the contract is for the entire building. Specifically, the request asked (a) about the identification of performance obligations in the contract and (b) for each performance obligation identified, whether the real estate developer (entity) recognises revenue over time or at a point in time.

Identifying performance obligations in the contract

Applying paragraphs 22–30 ~~of IFRS 15~~, an entity identifies as a performance obligation each promise to transfer to the customer 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.

Paragraph 27 ~~of IFRS 15~~ specifies that a good or service promised to a customer is distinct if (a) the customer can benefit from the good or service on its own or together with other resources readily available to the customer (ie the good or service is capable of being distinct); and (b) the entity's promise to transfer the good or service is separately identifiable from other promises in the contract (ie the promise to transfer the good or service is distinct within the context of the contract). The assessment of the criteria in paragraph 27 requires judgement.

Paragraph BC100 ~~explains~~ notes that an entity assesses the criterion in paragraph 27(a) based on the characteristics of the goods or services themselves. Accordingly, an entity disregards any contractual limitations that might preclude the customer from obtaining readily available resources from a source other than the entity.

Paragraph 29 explains that the objective underlying the criterion in paragraph 27(b) is to determine whether the nature of the promise, within the context of the contract, is to transfer each of the promised goods or services individually or, instead, to transfer a combined item to which those goods or services are inputs. Paragraph 29 also specifies some factors that indicate that two or more promises to transfer goods or services are not separately identifiable.

The Board ~~explained~~ noted in paragraphs BC105, BC116J and BC116K that the notion of ‘separately identifiable’ in paragraph 27(b) is influenced by the notion of separable risks (ie whether the risk 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 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 considers the level of integration, interrelation or interdependence among the promises to transfer goods or services. 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.

Application of paragraph 27 to the fact pattern in the request

A real estate contract for the transfer of land and a building

~~The identification of performance obligations in a contract requires an entity to assess the particular facts and circumstances of the contract. The Committee observed that that assessment may involve judgement and the outcome depends on those particular facts and circumstances.—~~

In a real estate contract that involves the transfer of land and of a building that the entity constructs on that land, the entity is required to identify the performance obligations in the contract. The following paragraphs outline factors to consider in assessing whether the entity identifies the promise to transfer land as a separate

performance obligation; those paragraphs do not consider whether the entity identifies one or more performance obligations in relation to the transfer of the building.

~~In the fact pattern described in the request, the land and the building are each capable of being distinct and thus the Committee observed that~~ When assessing the criterion in paragraph 27(a) is met. The, the entity assesses whether the customer could benefit from the land on its own or together with other resources readily available to it. For example, could the customer could hire another developer to construct a building on the land?; Similarly, could the customer could benefit from the construction of the building on its own or together with other resources readily available to it?; For example, could the customer could obtain the construction services from the entity or another developer without any transfer of land?;

When assessing the criterion in paragraph 27(b) and its underlying objective explained in paragraph 29—(ie determining whether the nature of the promise, within the context of the contract, is to transfer the land and the building individually or, instead, to transfer a combined item to which the land and building are inputs), the Committee observed that the entity considers the following:

- a. Is there a transformative relationship between the transfer of the land and the construction of the building in the process of fulfilling the contract? ~~In other words~~ For example, would the entity's performance in constructing the building be any different ~~had the customer already purchased if it did not also transfer the land from another party~~ and vice versa? There is a functional relationship between the land and the building—the building cannot exist without the land; its foundations will be built into the land. However, this does not necessarily mean that the risks ~~to which the entity is exposed~~ assumes in transferring the land to the customer are inseparable from the risks it assumes in ~~of~~ constructing the building.
- b. would the entity be able to fulfil its promise to transfer the land even if ~~the customer purchased the construction services from another developer~~ it did not construct the building, and would it be able to fulfil its promise to construct the building even if it did not transfer the land ~~the customer had purchased the land from another party?~~

The Committee ~~observed~~ concluded that the promise to transfer the land would be separately identifiable from the promise to construct the building on that land if the entity concluded that (a) its performance in constructing the building would be the same regardless of whether ~~the customer had purchased~~ it also transferred the land ~~from it or another party~~; and (b) it would be able to fulfil its promise to construct the building even if ~~the customer had purchased~~ it did not also transfer the land ~~from another party~~, and would be able to fulfil its promise to transfer the land even if it did not also construct the building ~~the customer purchased the construction services from another developer~~.

~~In the fact pattern described in the request, the Committee observed that this would be the case and, thus, concluded that there are two performance obligations in the contract—ie a promise to transfer the land to the customer and a promise to construct the building on that land.—~~

Applying ~~ication~~ of paragraph 35 of IFRS 15 to the fact pattern in the request

~~For each performance obligation, the entity applies the criteria in paragraph 35 of IFRS 15 to determine whether to recognise revenue over time. If none of the criteria in paragraph 35 are met, the entity recognises revenue at a point in time.~~

Paragraph 35 specifies that an entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if any one (or more) of the three criteria in paragraph 35 is met. Paragraph 32 states that if an entity does not satisfy a performance obligation over time, it satisfies the performance obligation at a point in time. Accordingly, the Committee observed that, at contract inception for each performance obligation, an entity applies the criteria in paragraph 35 to determine whether it recognises revenue over time.

The Committee has included explanatory information about the application of paragraph 35 to real estate contracts in its agenda decision ‘Revenue Recognition in a Real Estate Contract’ published in March 2018.

The Committee concluded that the principles and requirements in IFRS 15 provide an adequate basis for an entity to recognise revenue in the fact pattern described in the

request. Consequently, the Committee [decided] not to add this matter to its standard-setting agenda.

Application of paragraph 35 to the fact pattern in the request

The identification of performance obligations in a contract and the assessment of whether to recognise revenue over time or at a point in time requires an assessment of the particular facts and circumstances of the contract, taking into account the legal environment within which the contract is enforceable. Accordingly, the outcome of an entity's assessment depends on those particular facts and circumstances.

In the fact pattern described in the request, the contract includes the following features:

- a. the entity and the customer enter into a non-cancellable contract for the sale of a building yet to be constructed by the entity that will comprise residential units.
The contract is for the sale of the entire building.
- b. at contract inception, the entity irrevocably transfers to the customer legal title to the land on which the entity will construct the building. The contract specifies a price for the land, which the customer pays on signing the contract.
- c. the entity and the customer agree upon the structural design and specification of the building before the contract is signed. As the building is being constructed:
 - i. if the customer requests changes to the structural design or specification, the entity prices the proposed changes based on a methodology specified in the contract; the customer then decides whether to proceed with the changes. The entity can reject the customer's request for changes only for a limited number of reasons, such as when the change would breach planning permission.
 - ii. the entity can request changes to the structural design or specification only if not doing so would lead to an unreasonable increase in costs or delay to construction. The customer must approve those changes.
- d. the customer is required to make milestone payments throughout the construction period. However, these payments do not necessarily correspond to the amount of work completed to date.

It is assumed that (i) all the criteria in paragraph 9 are met and (ii) the entity identifies two performance obligations applying paragraphs 22-30—a promise to transfer the land to the customer and a promise to construct the building on that land.

Application of paragraph 35 to the promise to transfer land

~~In the fact pattern described in the request, t~~ The entity's performance delivers transfers the land to the customer. The land is not consumed immediately and, thus, the criterion in paragraph 35(a) is not met. Nor does the entity's performance create or enhance the land, and, thus, the criteria in paragraphs 35(b) and 35(c) are not met.

Consequently, ~~the Committee observed that~~ the entity recognises revenue for the transfer of the land to the customer at a point in time applying paragraph 38 of IFRS 15.

Application of paragraph 35 to the promise to construct the building

~~The Committee discussed the application of paragraph 35 to a promise to construct a real estate unit in [September 2017]. The following observations made by the Committee in its [tentative] agenda decision 'Revenue recognition in a real estate contract (IFRS 15)' are also applicable to the promise to construct the building in the fact pattern described in the request:¹~~

- ~~a. in a contract for the sale of a building that the entity constructs, the Committee observed that paragraph 35(a) is not applicable because the entity's performance creates an asset, ie the building, that is not consumed immediately.~~
- ~~b. paragraph BC129 of IFRS 15 explains that the Board included the criterion in paragraph 35(b) 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'. Accordingly, the Committee observed that, in applying paragraph 35(b), an entity assesses whether there is evidence that the customer clearly controls the asset that is being created or enhanced (for example, the part-constructed building) as it is created or enhanced. An entity considers all relevant factors in making this assessment—no one factor is determinative.~~

~~e. in applying paragraph 35(b), it is important to apply the requirements for control to the asset that the entity's performance creates or enhances. In a contract for the sale of a building that the entity constructs, the asset created is the building itself. It is not, for example, the right to obtain the building in the future.~~

~~[The paragraph above will be updated depending on the outcome of the Committee's consideration of comment letters received on the IFRS 15 tentative agenda decision published in September 2017.]~~

~~In the fact pattern described in the request discussed in November 2017, the Committee observed that the criterion in paragraph 35(a) is not met. This is because t~~

The criterion in paragraph 35(a) is not met because the entity's performance creates an asset that is not consumed immediately.

Paragraph 35(b)

In assessing the criterion in paragraph 35(b), the entity assesses whether, as the building is being constructed, the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the part-constructed building.

~~The Committee concluded that, in the fact pattern described in the request, the customer controls the part-constructed building as it is being constructed because the customer has the following:~~

- a. the ability to direct the use of the building as it is being constructed. The customer has this ability through its control of the land, and by being able to change the structural design and specification of the building as it is being constructed. The contract also enables the customer to prevent the entity or others from directing the use of the building.
- b. the ability to obtain substantially all of the remaining economic benefits from the building. The entity cannot redirect the building for another use or to another entity. Accordingly, on signing the contract, the customer has the ability to obtain substantially all of the remaining benefits from the building. The contract also enables the customer to prevent the entity or others from obtaining the benefits from the building.

Accordingly, the criterion in paragraph 35(b) is met. ~~The Committee noted~~ The Board ~~observed~~ ’s observation in paragraph BC129 of IFRS 15 that ‘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’.

Appendix B—Proposed wording for agenda decision

B1. This appendix includes the proposed wording for the agenda decision in Appendix A but with no mark-up.

Revenue Recognition in a Real Estate Contract that Includes the Transfer of Land (IFRS 15 *Revenue from Contracts with Customers*)

The Committee received a request about revenue recognition in a contract for the sale of land and a building to be constructed on the land. The land represents all of the area on which the building will be constructed and the contract is for the entire building. Specifically, the request asked (a) about the identification of performance obligations in the contract and (b) for each performance obligation identified, whether the real estate developer (entity) recognises revenue over time or at a point in time.

Identifying performance obligations in the contract

Applying paragraphs 22–30, an entity identifies as a performance obligation each promise to transfer to the customer 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.

Paragraph 27 specifies that a good or service promised to a customer is distinct if (a) the customer can benefit from the good or service on its own or together with other resources readily available to the customer (ie the good or service is capable of being distinct); and (b) the entity’s promise to transfer the good or service is separately identifiable from other promises in the contract (ie the promise to transfer the good or service is distinct within the context of the contract). The assessment of the criteria in paragraph 27 requires judgement.

Paragraph BC100 notes that an entity assesses the criterion in paragraph 27(a) based on the characteristics of the goods or services themselves. Accordingly, an entity disregards any contractual limitations that might preclude the customer from obtaining readily available resources from a source other than the entity.

Paragraph 29 explains that the objective underlying the criterion in paragraph 27(b) is to determine whether the nature of the promise, within the context of the contract, is to

transfer each of the promised goods or services individually or, instead, to transfer a combined item to which those goods or services are inputs. Paragraph 29 also specifies some factors that indicate that two or more promises to transfer goods or services are not separately identifiable.

The Board noted in paragraphs BC105, BC116J and BC116K that the notion of ‘separately identifiable’ in paragraph 27(b) is influenced by the notion of separable risks (ie whether the risk 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 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 considers the level of integration, interrelation or interdependence among the promises to transfer goods or services. 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.

A real estate contract for the transfer of land and a building

In a real estate contract that involves the transfer of land and of a building that the entity constructs on that land, the entity is required to identify the performance obligations in the contract. The following paragraphs outline factors to consider in assessing whether the entity identifies the promise to transfer land as a separate performance obligation; those paragraphs do not consider whether the entity identifies one or more performance obligations in relation to the transfer of the building.

When assessing the criterion in paragraph 27(a), the entity assesses whether the customer could benefit from the land on its own or together with other resources readily available to it. For example, could the customer hire another developer to construct a building on the land? Similarly, could the customer benefit from the construction of the building on its own or together with other resources readily

available to it? For example, could the customer obtain the construction services from the entity or another developer without any transfer of land?

When assessing the criterion in paragraph 27(b) and its underlying objective explained in paragraph 29 (ie determining whether the nature of the promise, within the context of the contract, is to transfer the land and the building individually or, instead, to transfer a combined item to which the land and building are inputs), the Committee observed that the entity considers the following:

- a. is there a transformative relationship between the transfer of the land and the construction of the building in the process of fulfilling the contract? For example, would the entity's performance in constructing the building be any different if it did not also transfer the land and vice versa? There is a functional relationship between the land and the building—the building cannot exist without the land; its foundations will be built into the land. However, this does not necessarily mean that the risks the entity assumes in transferring the land to the customer are inseparable from the risks it assumes in constructing the building.
- b. would the entity be able to fulfil its promise to transfer the land even if it did not construct the building, and would it be able to fulfil its promise to construct the building even if it did not transfer the land?

The Committee concluded that the promise to transfer the land would be separately identifiable from the promise to construct the building on that land if the entity concluded that (a) its performance in constructing the building would be the same regardless of whether it also transferred the land; and (b) it would be able to fulfil its promise to construct the building even if it did not also transfer the land, and would be able to fulfil its promise to transfer the land even if it did not also construct the building.

Applying paragraph 35 of IFRS 15

Paragraph 35 specifies that an entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if any one (or more) of the three criteria in paragraph 35 is met. Paragraph 32 states that if an entity does not satisfy a performance obligation over time, it satisfies the

performance obligation at a point in time. Accordingly, the Committee observed that, at contract inception for each performance obligation, an entity applies the criteria in paragraph 35 to determine whether it recognises revenue over time.

The Committee has included explanatory information about the application of paragraph 35 to real estate contracts in its agenda decision ‘Revenue Recognition in a Real Estate Contract’ published in March 2018.

The Committee concluded that the principles and requirements in IFRS 15 provide an adequate basis for an entity to recognise revenue in the fact pattern described in the request. Consequently, the Committee decided not to add this matter to its standard-setting agenda.

Application of paragraph 35 to the fact pattern in the request

The identification of performance obligations in a contract and the assessment of whether to recognise revenue over time or at a point in time requires an assessment of the particular facts and circumstances of the contract, taking into account the legal environment within which the contract is enforceable. Accordingly, the outcome of an entity’s assessment depends on those particular facts and circumstances.

In the fact pattern described in the request, the contract includes the following features:

- a. the entity and the customer enter into a non-cancellable contract for the sale of a building yet to be constructed by the entity that will comprise residential units.
The contract is for the sale of the entire building.
- b. at contract inception, the entity irrevocably transfers to the customer legal title to the land on which the entity will construct the building. The contract specifies a price for the land, which the customer pays on signing the contract.
- c. the entity and the customer agree upon the structural design and specification of the building before the contract is signed. As the building is being constructed:
 - i. if the customer requests changes to the structural design or specification, the entity prices the proposed changes based on a methodology specified in the contract; the customer then decides whether to proceed with the changes. The entity can reject the customer’s request for changes only for

a limited number of reasons, such as when the change would breach planning permission.

- ii. the entity can request changes to the structural design or specification only if not doing so would lead to an unreasonable increase in costs or delay to construction. The customer must approve those changes.
- d. the customer is required to make milestone payments throughout the construction period. However, these payments do not necessarily correspond to the amount of work completed to date.

It is assumed that (i) all the criteria in paragraph 9 are met and (ii) the entity identifies two performance obligations applying paragraphs 22-30—a promise to transfer the land to the customer and a promise to construct the building on that land.

Application of paragraph 35 to the promise to transfer land

The entity's performance transfers the land to the customer. The land is not consumed immediately and, thus, the criterion in paragraph 35(a) is not met. Nor does the entity's performance create or enhance the land, and, thus, the criteria in paragraphs 35(b) and 35(c) are not met.

Consequently, the entity recognises revenue for the transfer of the land to the customer at a point in time applying paragraph 38 of IFRS 15.

Application of paragraph 35 to the promise to construct the building

The criterion in paragraph 35(a) is not met because the entity's performance creates an asset that is not consumed immediately.

Paragraph 35(b)

In assessing the criterion in paragraph 35(b), the entity assesses whether, as the building is being constructed, the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the part-constructed building.

The customer controls the part-constructed building as it is being constructed because the customer has the following:

- a. the ability to direct the use of the building as it is being constructed. The customer has this ability through its control of the land, and by being able to change the structural design and specification of the building as it is being constructed. The contract also enables the customer to prevent the entity or others from directing the use of the building.
- b. the ability to obtain substantially all of the remaining economic benefits from the building. The entity cannot redirect the building for another use or to another entity. Accordingly, on signing the contract, the customer has the ability to obtain substantially all of the remaining benefits from the building. The contract also enables the customer to prevent the entity or others from obtaining the benefits from the building.

Accordingly, the criterion in paragraph 35(b) is met. The Board observed in paragraph BC129 that ‘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’.