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## IASB<sup>®</sup> meeting

Date	<b>February 2024</b>
Project	<b>Second Comprehensive Review of the <i>IFRS for SMEs</i><sup>®</sup> Accounting Standard</b>
Topic	<b>Proposed revised Section 23 <i>Revenue from Contracts with Customers</i>—Redeliberation topics</b>
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This paper has been prepared for discussion at a public meeting of the International Accounting Standards Board (IASB). This paper does not represent the views of the IASB or any individual IASB member. Any comments in the paper do not purport to set out what would be an acceptable or unacceptable application of IFRS<sup>®</sup> Accounting Standards or the *IFRS for SMEs*<sup>®</sup> Accounting Standard. The IASB's technical decisions are made in public and are reported in the IASB<sup>®</sup> *Update*.

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## Introduction

1. The International Accounting Standards Board (IASB) proposed to revise Section 23 *Revenue* of the *IFRS for SMEs* Accounting Standard to align it with IFRS 15 *Revenue from Contracts with Customers* in the Exposure Draft *Third edition of the IFRS for SMEs Accounting Standard* (Exposure Draft). This paper discusses eight topics where stakeholders requested changes to, or raised concerns about, the requirements proposed in the Exposure Draft.
2. In this paper, the term SMEs refers to entities that are eligible to apply the *IFRS for SMEs* Accounting Standard.

## Purpose of the paper

3. The purpose of this paper is to ask the IASB:
  - (a) to consider feedback on eight topics where stakeholders requested changes to, or raised concerns about, the requirements proposed in Section 23 *Revenue from Contracts with Customers* of the Exposure Draft; and
  - (b) to decide whether to change the requirements proposed in the Exposure Draft.

## Staff recommendations

4. The staff recommendations are summarised in Table 1 of this paper.

**Table 1—Summary of recommended changes to Section 23 *Revenue from Contracts with Customers* of the Exposure Draft**

Topic	Recommended change(s) to the requirements proposed in the Exposure Draft	Paragraph reference
<b><i>Change the proposed requirements</i></b>		
Contract modifications	<ul style="list-style-type: none"> <li>Remove the option for an SME to account for a contract modification as a separate contract if the modification meets the criteria in paragraph 23.15(a)–(b) of the Exposure Draft (that is, remove the simplification proposed in the Exposure Draft)</li> <li>Instead, require an SME to account for a contract modification as a separate contract if the modification meets the criteria in paragraph 23.15(a)–(b) of the Exposure Draft.</li> </ul>	18–23
Customer options for additional goods or services	<ul style="list-style-type: none"> <li>Remove the requirement for an SME to determine if the effect of accounting for an option that provides a material right to a customer as a separate promise is significant to the individual contract (that is, remove the simplification proposed in the Exposure Draft)</li> <li>Instead, require an SME to account for an option that provides a material right to a customer as a separate promise, unless doing so involves undue cost or effort.</li> </ul>	24–44
Costs to obtain a contract	<ul style="list-style-type: none"> <li>Remove the requirement for an SME to recognise the incremental costs of obtaining a contract as an asset if the SME can identify and assess the costs as recoverable without undue cost or effort (that is, remove the simplification proposed in the Exposure Draft)</li> <li>Instead, require an SME to recognise costs to obtain a contract as an expense when incurred.</li> </ul>	45–64

<b><i>Retain the proposed requirements</i></b>		
Performance obligation/promise terminology		65–86
Measuring variable consideration		87–104
<b><i>Retain the proposed requirements with drafting changes</i></b>		
Non-cash consideration	<ul style="list-style-type: none"> <li>• Include the term ‘barter’ in the description of non-cash consideration; and</li> <li>• Present separately: <ul style="list-style-type: none"> <li>– the requirement to measure the fair value of non-cash consideration; and</li> <li>– the exemption from the requirement to measure the fair value of non-cash consideration.</li> </ul> </li> </ul>	105–114
Allocation based on stand-alone selling prices	Include guidance on methods for estimating the standalone selling price in separate educational material instead of the revised Section 23.	115–125
Allocating variable consideration	Combine the requirements for allocating variable consideration and discounts.	126–136

## Structure of the paper

5. This paper is structured as follows:
  - (a) background (paragraphs 7–16);
  - (b) redeliberation topics (paragraphs 17–136); and
  - (c) next steps (paragraph 137); and
  - (d) Appendix—Figures illustrating the recommended change to the proposed requirements for contract modifications.
6. This paper includes eight questions for the IASB; questions for the IASB are included at the end of the staff analysis for each topic.

## Background

7. Section 23 of the *IFRS for SMEs* Accounting Standard sets out the requirements for accounting for revenue and is based on IAS 11 *Construction Contracts* and IAS 18 *Revenue*. The Section requires revenue to be recognised for goods when risks and rewards are transferred and, for services, as the service is performed.
8. In 2014, the IASB issued IFRS 15, which replaced IAS 11 and IAS 18. IFRS 15 introduced a single framework for recognising revenue for both goods and services. IFRS 15 requires revenue to be recognised when the customer obtains control of the good or service.
9. In the Exposure Draft, the IASB proposed amendments to the *IFRS for SMEs* Accounting Standard to align it with IFRS 15. To do so, the IASB proposed revising Section 23 of the *IFRS for SMEs* Accounting Standard to reflect the principles and language used in IFRS 15. The IASB also proposed simplifications to the requirements in IFRS 15 to reduce costs for SMEs of applying the revised Section 23.

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10. Feedback was provided on Section 23 of the Exposure Draft through comment letters and outreach events. Fieldwork on the Section was also carried out with accounting practitioners involved in the preparation of SMEs' financial statements. The feedback generally agreed with the IASB's proposals to revise Section 23 of the *IFRS for SMEs* Accounting Standard to align it with IFRS 15. However, stakeholders had concerns about some of the proposals.
  11. Stakeholders identified topics where they would like the proposed requirements to be:
    - (a) simplified further; or
    - (b) the same as IFRS 15 (that is, not simplified).
  12. Some stakeholders also had general concerns that the revised Section 23 was too long and complex for SMEs. A few comment letter respondents (respondents) had concerns that the IASB was not considering insights from the IASB's post-implementation review (PIR) of IFRS 15 as it developed its proposals for the *IFRS for SMEs* Accounting Standard.
  13. At its meeting in October 2023, the IASB considered feedback on the proposals in the Exposure Draft to revise Section 23 of the *IFRS for SMEs* Accounting Standard to align it with IFRS 15. The IASB decided to proceed with revising Section 23 of the Standard to reflect the principles in IFRS 15.<sup>1</sup> The IASB also discussed how to respond to stakeholder's concerns about the proposals.
  14. To respond to concerns about specific requirements in the proposed revised Section 23, the staff suggested the IASB redeliberate topics where stakeholders had requested changes to, or raised concerns about, the requirements.<sup>2</sup> This paper discusses eight of the 15 topics suggested by the staff.

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<sup>1</sup> See [IASB Update](#) from the October 2023 IASB meeting.

<sup>2</sup> The redeliberation topics are summarised in the appendix to [Agenda Paper 30A Proposed revised Section 23 Revenue from Contracts with Customers](#) of the October 2023 IASB meeting.

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15. To respond to concerns about the length and complexity of the proposed revised Section 23, the staff suggested exploring ways to:
    - (a) reduce the length of the proposed revised Section 23, and
    - (b) use plainer language to express the requirements in the proposed revised Section 23.
  
  16. To respond to concerns about the interaction between the project and the PIR of IFRS 15, the staff suggested drawing on relevant feedback from the PIR during the IASB's future discussions on the revised Section 23. This paper references information gathered during the PIR of IFRS 15.

## Redeliberation topics

17. For each topic, the paper provides:
  - (a) a description of the requirements in the Exposure Draft;
  - (b) a summary of the feedback received;
  - (c) staff analysis of the feedback; and
  - (d) a staff recommendation on whether and how to change the proposed revised Section 23.

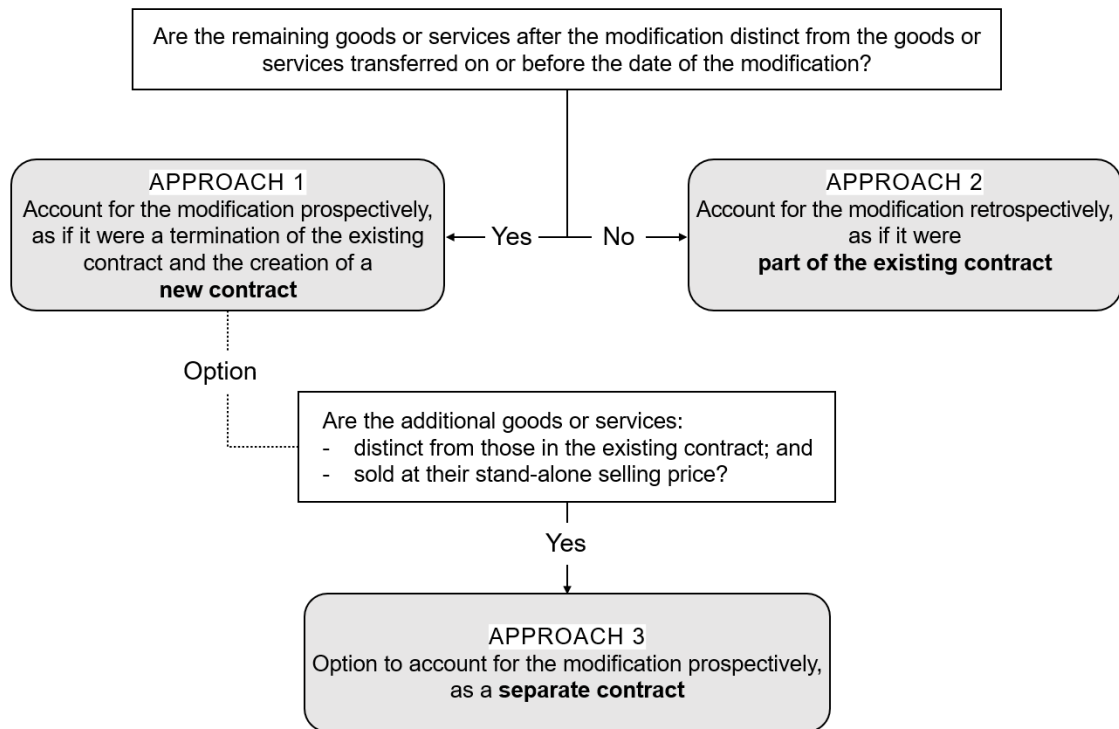
### ***Contract modifications***

18. The IASB proposed three different approaches for accounting for contract modifications in the Exposure Draft.<sup>3</sup> Each approach was subject to criteria. If a modification could be accounted for by terminating the contract and creating a new contract, SMEs were given the option to account for the modification as an additional, separate contract if specified criteria were met. The requirements proposed in the Exposure Draft are illustrated in Figure 1 of this paper.

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<sup>3</sup> Paragraphs 23.14–23.15 of the Exposure Draft.

**Figure 1—Summary of the requirements for contract modifications proposed in the Exposure Draft**



19. The option to account for a contract modification as a separate contact (Approach 3 in Figure 1) was considered a simplification compared to the requirements for accounting for contract modifications in IFRS 15. No such option exists in IFRS 15. An entity applying IFRS 15 must account for a contract modification as a separate contract if it meets specified criteria. If not, the entity must determine whether the goods or services not yet transferred at the date of the modification are distinct from the goods or services transferred on or before the date of the modification.<sup>4</sup>

*Feedback received*

20. Among fieldwork participants unfamiliar with IFRS 15, there were comparable numbers who were able to identify how to account for contract modifications and who were not. Many participants who were unable to identify how to account for a contract

<sup>4</sup> Paragraphs 20–21 of IFRS 15.

modification said the requirements proposed in the Exposure Draft were unclear and difficult to understand.

### *Staff analysis*

21. When the IASB developed the Exposure Draft, it considered whether it would be possible to reduce the number of approaches and criteria that SMEs must consider when accounting for contract modifications by removing the requirement in IFRS 15 to account for a contract modification as a separate contract (Approach 3 in Figure 1). However, the requirement was retained because Approach 3 would often be the easiest way for an entity to account for a contract modification. Consequently, all three approaches for accounting for contract modifications in IFRS 15 were included in the Exposure Draft. However, the IASB decided to make Approach 3 an option so it was easier for SMEs to identify which approach to use. By making Approach 3 an option, SMEs would be required to consider two approaches instead of three.
22. The IASB has generally restricted accounting policy options in the *IFRS for SMEs* Accounting Standard because including more options generally increases complexity and reduces comparability. The staff believe the option to apply Approach 3 has made the proposed requirements difficult for SMEs to understand. Consequently, the staff recommend all three approaches for accounting for contract modifications are included in the revised Section 23 and are mandatory, not optional. SMEs would be *required* to apply Approach 3 if the modification meets the specified criteria, instead of having the *option* to do so. This would align the requirements for accounting for contract modification in Section 23 with the requirements in IFRS 15. The recommended change to the proposed requirements is illustrated in the appendix to this paper.
23. The SMEIG considered the staff recommendation in paragraph 22 of this paper when it met in December 2023. SMEIG members generally agreed with the recommendation. However, some SMEIG members said the option for SMEs to apply Approach 3 should be retained because it gives SMEs flexibility in how to account for



contract modifications (that is, SMEs have the option to apply Approach 1 instead of Approach 3). In circumstances when an SME meets the criteria to apply Approach 3, doing so would often be easier than applying Approach 1. As SMEs are expected to choose to apply the easier approach, the flexibility is expected to be of little benefit to SMEs.

#### Question for the IASB

1. Does the IASB agree to require an SME to account for a contract modification as a separate contract if the modification meets the criteria in paragraph 23.15(a)–(b) of the Exposure Draft, therefore aligning the requirements for contract modifications in the *IFRS for SMEs* Accounting Standard with those in IFRS 15?

#### ***Customer options for additional goods or services***

24. An entity may grant a customer an option to acquire additional goods or services for free or at a discount (for example, sales incentives, customer award credits or other discounts on future goods or services). An entity applying IFRS 15 must account for the option as a separate performance obligation if the option provides a material right to the customer that it would not receive without entering into that contract (referred to as a material right).<sup>5</sup> To account for a material right, IFRS 15 requires an entity to estimate the stand-alone selling price of the option, allocate the transaction price based on this amount and recognise revenue when those future goods or services are transferred or when the option expires.<sup>6</sup>
25. The IASB proposed requirements in the Exposure Draft similar to those described in paragraph 24 of this paper. However, the IASB proposed that an SME would account for an option that provides a material right as a separate promise only if the effect of doing so is significant to the accounting for the individual contract (the proposed simplification).<sup>7</sup>

<sup>5</sup> Paragraph B40 of IFRS 15.

<sup>6</sup> Paragraphs B40 and B42 of IFRS 15.

<sup>7</sup> Paragraph 23.35 of the Exposure Draft.

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*Feedback received*

26. Some respondents (mostly accounting bodies) who commented on Section 23 said applying the proposed simplification would involve substantial judgement and add complexity to the Standard. Some respondents (mostly accounting firms and accounting bodies) asked for guidance and illustrative examples to help SMEs apply the simplification. One respondent said the simplification would prevent SMEs accounting for options that are significant on a cumulative basis but are not individually significant (for example customer award credits or points).

*Staff analysis****Proposed simplification***

27. The feedback indicates that the proposed simplification would add complexity to the *IFRS for SMEs* Accounting Standard. Part of the complexity is because the simplification requires SMEs to differentiate between the concepts of significance and materiality to assess two related items. The staff do not think additional guidance or illustrative examples can overcome the complexity of these judgements. Consequently, the staff do not recommend including the proposed simplification in the revised Section 23.

***Cost benefit considerations***

28. The proposed simplification was intended to avoid SMEs incurring substantial costs to account for options that are not material to their financial statements. Therefore, the simplification was introduced for cost-benefit reasons.
29. It can be costly for entities to separately account for material rights because of the systems needed to capture information about customer options. Accounting software packages used by SMEs can be integrated with systems that record and track customer options. However, these systems rely on SMEs maintaining information about their customers and their interactions with them. Feedback from fieldwork participants

indicates that SMEs do not typically have systems that capture information about customer options if:

- (a) customers are not expected to return and exercise the options (that is, the options are expected to expire); or
- (b) the additional goods or services associated with the options are low-value and relate to a large volume of contracts.

30. In the instances described in paragraph 29(a)–(b) of this paper, if SMEs do not have systems that capture information about customer options, it is presumed that the cost and effort of developing and maintaining such systems would outweigh the usefulness of the information in helping SMEs run their business. This is to do with both the systems and the nature of the options, which are expected to expire or relate to low-value goods and services.
31. If an entity does not separately account for material rights, the entity recognises revenue attributed to the additional goods and services associated with an option when the other promises in the contract are satisfied, instead of when the additional goods or services are transferred or when the option expires. Therefore, the entity would recognise the revenue attributable to the additional goods or services prematurely. In the instances described in paragraph 29(a)–(b) of this paper, the options are expected to expire or relate to low-value goods. Therefore, the revenue attributable to these options would be small and separately accounting for the material rights would not be expected to significantly change the timing of revenue recognised.
32. Separately accounting for material rights in the instances described in paragraph 29(a)–(b) of this paper would mean an SME's obligations would be more faithfully represented than if the SME did not separately account for the rights. However, if an SME did not have a system that captured the information to separately account for material rights, the incremental costs and additional effort of doing so are unlikely to exceed the benefits of this information to users of the SME's financial statements.

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***Application of materiality***

33. As discussed in paragraph 28 of this paper, the intention of the proposed simplification was to avoid SMEs accounting for immaterial transactions. SMEs can avoid accounting for immaterial transaction by making materiality judgements. However, it can be difficult for entities to make materiality judgements about customer options because:
- (a) entities must assess materiality for two related items from two different perspectives. That is, whether an option provides a customer with a material right; and whether separately accounting for the material right would provide material information. This requires an entity to assess materiality from the perspective of its customers and the users of its financial statements.
  - (b) assessing whether customer options are quantitatively material can require entities to perform complex calculations based on estimates. Doing so requires entities to maintain systems that capture information about customer options. A few respondents to the [Request for Information Post-implementation Review of IFRS 15 Revenue from Contracts with Customers](#) (Request for Information) said such assessments can lead to significant ongoing costs for some entities with numerous multi-element contracts.<sup>8</sup>
34. Entities do not consider the cost or effort of applying a requirement when they make materiality judgements. However, SMEs consider these factors when they assess whether to apply an undue cost or effort exemption.
35. An undue cost or effort exemption would provide SMEs with a straightforward and structured way of assessing the effect on users of separately accounting for material rights. The exemption would also avoid SMEs having to separately accounting for material rights when this involves undue cost or effort. This would address concerns

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<sup>8</sup> The [Norwegian Accounting Standards Board Response](#) to Question 1(c) of the IASB's [Request for Information Post-implementation Review of IFRS 15 Revenue from Contracts with Customers](#) (Request for Information) and paragraph 7 of [EFRAG's Comment Letter](#) on the Request for Information.

about SMEs that do not have systems that capture information about customer options, discussed in paragraph 29 of this paper.

36. Consequently, the staff recommend that SMEs are required to account for a material right as a separate promise unless doing so involves undue cost or effort. SMEs that use the undue cost or effort exemption would disclose that fact and the reasons why accounting for a material right as a separate promise would involve undue cost or effort (consistent with paragraph 2.14D of the *IFRS for SMEs* Accounting Standard). The SMEIG considered the recommendation when it met in December 2023. SMEIG members generally agreed with the recommendation.
37. The application of the recommended undue cost or effort exemption is discussed in paragraphs 38–44 of this paper.

#### ***Renewal options***

38. An entity may grant a customer the option to renew a contract on similar terms (a renewal option). The Exposure Draft distinguishes renewal options from other options for additional goods or services because the proposed requirements for measuring renewal options are simplified compared with other options.<sup>9</sup>
39. Renewal options are typically offered by entities with subscription-based or membership-based business models. As customers renewals are a key driver of profitability in entities with these business models, entities would be expected to have systems that capture information about customer renewals. Consequently, the staff initially suggested excluding renewal options from the scope of the undue cost of effort exemption. The SMEIG considered the suggestion when it met in December 2023. A SMEIG member disagreed with the suggestion and said the undue cost or effort exemption would be necessary for SMEs that do not have systems that record information about customer renewals because they are not fundamental to the SMEs' business.

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<sup>9</sup> Paragraph 23.36 of the Exposure Draft.

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40. Renewal options are offered to incentivise repeat custom. However, renewal options are not restricted to entities with subscription-based or membership-based business models. Consequently, the staff do not recommend restricting the scope of the undue cost or effort exemption.

***Options redeemed cumulatively***

41. Some customer options are redeemed on a cumulative basis (for example customer award credits or points). Each option arises from a single contract, but to exercise the options, customers may need to combine options from several contracts.
42. The undue cost or effort exemptions in the *IFRS for SMEs Accounting Standard* are based on an SME's assessment of complying with a requirement when it is applied to an individual transaction.<sup>10</sup> Consequently, an SME's undue cost or effort assessment would be based on the benefits to users of separately accounting for options that arise from an individual contract with a customer. If the assessment included options from other contracts with the customer, the assessment may be different.
43. Separately accounting for customer options can be costly for SMEs because they do not have systems that capture information about customer options. The cost of such a system is expected to be similar if an SME had to separately account for options that arise from a single contract with a customer or all contracts with its customers. Consequently, if an SME applies the undue cost or effort exemption to options that arise from one contract, it is likely that the SME would also apply the exemption if it had to assess the cost or effort of separately accounting for all options that arise from all contracts with customers (that is, the conclusion would be the same regardless of whether the assessment was based on one contract or all contracts).
44. Based on the analysis in paragraph 43 of this paper, the staff do not recommend requiring SMEs to assess undue cost or effort differently when accounting for customer options that are redeemed cumulatively. Consequently, an SME's undue

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<sup>10</sup> Paragraphs 2.14A–2.14D of the *IFRS for SMEs Accounting Standard*.

cost and effort assessment would be based on separately accounting for options that arise from individual contracts with customers. There would be no exception to the undue cost or effort exemption for customer options that are redeemed cumulatively.

#### Question for the IASB

2. Does the IASB agree to require an SME to account for an option that provides a material right to a customer as a separate promise, unless doing so involves undue cost or effort?

#### ***Costs to obtain a contract***

45. The Exposure Draft proposed requiring SMEs to recognise costs incurred to obtain a contract with a customer as an asset if:
- (a) the costs would not have been incurred by the SME if the contract had not been obtained; and
  - (b) the costs are expected to be recovered.<sup>11</sup>
46. Under these proposals, SMEs would have been allowed to recognise costs to obtain a contract that meet the criteria in paragraph 45 of this paper as an expense if the amortisation period of the asset that the SME otherwise would have recognised is one year or less.<sup>12</sup>
47. SMEs would have been required to recognise costs that do not meet the criterion in paragraph 45(a) of this paper as an asset if the costs are explicitly chargeable to the customer regardless of whether the contract is obtained.<sup>13</sup>
48. The requirements proposed in the Exposure Draft for accounting for costs to obtain a contract are aligned with the requirements in IFRS 15<sup>14</sup>, except the Exposure Draft includes an undue cost or effort exemption. The proposed exemption allows an SME

<sup>11</sup> Paragraph 23.102 of the Exposure Draft.

<sup>12</sup> Paragraph 23.105 of the Exposure Draft.

<sup>13</sup> Paragraph 23.104 of the Exposure Draft.

<sup>14</sup> Paragraphs 91–94 of IFRS 15.

to recognise the costs to obtain a contract as an expense if the SME is unable to identify whether the costs meet the criteria in paragraph 45 of this paper without undue cost or effort.<sup>15</sup>

49. The proposed undue cost or effort exemption was intended for circumstances where the cost or effort of recognising costs to obtain a contract as an asset exceed the benefits of the information for users of the financial statements. These circumstances may arise in industries where the costs to obtain a contract relative to the costs of fulfilling the contract are small and not reflected in management's assessment of a contract's profit margin or a contract's pricing.

*Feedback received*

50. Some respondents (mostly accounting firms and accounting bodies) who commented on Section 23 of the Exposure Draft disagreed with the proposed undue cost or effort exemption. The respondents disagreed with the exemption because:
- (a) the exemption requires SMEs to apply judgement;
  - (b) SMEs must identify costs incurred to obtain a contract to apply the exemption, which can be the most difficult part of accounting for the costs; and
  - (c) SMEs are always expected to qualify to use the exemption. One respondent explained that this is because costs to obtain a contract are small for many SMEs.
51. All respondents who disagreed with the exemption suggested alternatives. Many of the respondents suggested that SMEs should have an accounting policy option to recognise costs to obtain a contract that meet the criteria in paragraph 45 of this paper as either an asset or an expense. Some respondents suggested that SMEs should be required to recognise costs to obtain a contract as an expense.

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<sup>15</sup> Paragraph 23.103 of the Exposure Draft.



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*Staff analysis*

52. Feedback suggests that SMEs would always use the proposed undue cost or effort exemption. This is because the cost or effort of applying the proposed requirements to recognise costs to obtain a contract as an asset would always exceed the benefits received by users of the financial statements of having this information (that is, complying with the requirements would always involve undue cost or effort).
53. One respondent explained that SMEs are expected to use the proposed exemption because the costs they incur to obtain contracts are small and the cost of applying the proposed requirements to recognise these costs as an asset would be high. An analysis of the financial statements of entities that apply IFRS 15 and recognise costs to obtain a contract as an asset shows that on average, the amount of costs amortised in the reporting period was less than 1% of the entities' total operating expenses.<sup>16</sup> Many of the entities where the amount of costs exceeded 1% operated in the telecommunications industry. Based on the analysis, costs incurred by SMEs to obtain contracts would also be expected to be small relative to their total costs.

*Users perspective*

54. To apply the proposed undue cost or effort exemption, an SME must consider how the economic decisions of those that are expected to use their financial statements could be affected by not recognising costs to obtain a contract as an asset.<sup>17</sup> No feedback was received from users about the requirements proposed in the Exposure Draft for accounting for costs to obtain a contract. However, one respondent suggested that SMEs should be required to recognise costs to obtain a contract as an expense because it better reflects the principle of simplicity. Applying the IASB's alignment principle

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<sup>16</sup> Based on a sample of 17 entities who filed their 2022 or 2023 financial statements with the Securities and Exchange Commission and disclosed the amount of costs to obtain a contract amortised during the reporting period (that is, the entities provided the information required by paragraph 128(b) of IFRS 15). Total operating costs were calculated using the classification of expenditure in the entities' income statements.

<sup>17</sup> See paragraph 2.14B of the *IFRS for SMEs Accounting Standard*.

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of simplicity involves considering simplifications for preparers and users of SMEs financial statements.<sup>18</sup>

55. Recognising costs to obtain a contract as an expense would mean all costs to obtain a contract are included in an SME's income statement in the period that they are incurred. This is different to the treatment proposed by the Exposure Draft, where costs to obtain a contract that meet certain criteria are recognised as an asset in the SME's statement of financial position. The asset comprises of costs incurred in different reporting periods and related to contracts obtained in different periods. For users of SMEs financial statements that have an interest in short-term cash flows, requiring SMEs to recognise costs to obtain a contract as an expense instead of an asset would provide greater transparency and more useful information.
56. Feedback about users' understanding of assets recognised from costs to obtain a contract was received as part of the PIR of IFRS 15. A few preparers from the telecommunications industry identified having to explain these assets to users of financial statements as an ongoing challenge of applying IFRS 15.<sup>19</sup> SMEs may have less sophisticated users of their financial statements compared with entities applying IFRS 15. Consequently, this challenge could be amplified for SMEs.

***Alternative approaches***

57. The proposed undue cost or effort exemption requires SMEs to make a judgement to determine if they can recognise costs to obtain a contract as an expense. Based on the above feedback and analysis, requiring SMEs to recognise costs to obtain a contract as an expense would:
- (a) remove unnecessary judgement from the Standard and make the revised Section 23 less burdensome for SMEs to apply; and
  - (b) provide information about costs to obtain a contract that is useful and understandable to users of SMEs' financial statements.

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<sup>18</sup> See paragraph BC31 of the Exposure Draft.

<sup>19</sup> Paragraph 10(a) of [Agenda Paper 6D Analysis of outreach feedback—Other areas](#) of the March 2023 IASB meeting.

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For these reasons, the staff recommend the proposed undue cost or effort exemption for accounting for costs to obtain a contract is not included in the revised Section 23. Instead, the staff recommend that SMEs are required to recognise costs to obtain a contract as an expense when incurred. For similar reasons, the staff also recommend the requirement for SMEs to recognise costs to obtain a contract that are explicitly recoverable from the customer as an asset regardless of whether the contract is obtained is not included in the revised Section 23.

58. The most common alternative approach suggested by respondents was to provide SMEs with an accounting policy option to recognise costs to obtain a contract that meet the criteria in paragraph 45 of this paper as either an asset or an expense. The SMEIG considered the suggestion when it met in July 2023. SMEIG members had mixed views on the suggestion.
59. The staff do not recommend that SMEs are provided with an accounting policy option to recognise costs to obtain a contract as an asset or an expense. If the IASB provided an accounting policy option, it would be making an exception to its general approach not to provide accounting policy options in the *IFRS for SMEs* Accounting Standard (as described in paragraph 22 of this paper). The staff think an exception for this topic is unnecessary because very few SMEs would be expected to choose to recognise costs to obtain a contract as an asset. Also, based on the analysis in paragraphs 55–56 of this paper, the option would also result in financial statements that are potentially less useful and less understandable to users of SMEs' financial statements.

#### **Disclosure**

60. The Exposure Draft proposed requiring SMEs to disclose the closing balance of assets recognised from the costs to obtain contracts and the amount of amortisation and any impairment losses recognised in the reporting period.<sup>20</sup> This disclosure would not be required as a consequence of the staff recommendation in paragraph 57 of this paper.

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<sup>20</sup> Paragraph 23.127 of the Exposure Draft.

61. The staff considered whether SMEs should disclose information about costs to obtain contracts as a consequence of the staff recommendation in paragraph 57 of this paper.
62. Identifying costs to obtain a contract can be subjective and involve significant judgement. Respondents said identifying the costs to obtain a contract was the most difficult part of accounting for these costs (see paragraph 50(b) of this paper). Feedback on identifying these costs was also received as part of the PIR of IFRS 15. A few stakeholders said identifying the costs was as an ongoing challenge of applying IFRS 15.<sup>21</sup>
63. For any disclosure about costs to obtain contracts to be useful, an SME would need to identify the costs to obtain contracts incurred in the period. This would be more burdensome than IFRS 15. This is because the exemption described in paragraph 46 of this paper means entities do not have to identify the costs to obtain a contract if the amortisation period for the asset that otherwise would have recognised is one year or less.
64. Consequently, the staff do not recommend that SMEs are required to disclose information about the costs to obtain a contract because of the costs and challenges to SMEs of doing so. The staff note that an SME could still disclose information about costs to obtain contracts if the SME determines that this information is relevant to users of its financial statements.

#### Question for the IASB

3. Does the IASB agree to require an SME to recognise costs to obtain a contract as an expense when incurred?

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<sup>21</sup> Paragraph 10(b) of [Agenda Paper 6D Analysis of outreach feedback—Other areas](#) of the March 2023 IASB meeting.

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***Performance obligation/promise terminology***

65. In IFRS 15, the term ‘performance obligation’ is used to identify the unit of account for the goods or services promised in a contract with a customer. The definition of a performance obligation in IFRS 15 is:

A promise in a contract with a customer to transfer to the customer either:

- (a) a good or service (or a bundle of goods or services) that is distinct; or
- (b) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.

66. The IASB used the term ‘promise’ in the Exposure Draft instead of the term ‘performance obligation’. The term ‘promise’ was considered to be more reflective of the language SMEs use to describe their obligations under contracts with customers. The proposed definition of a promise in the Exposure Draft was:

An obligation to transfer a good or service (or bundle of goods or services) that is distinct.

67. The proposed requirement to account for a series of distinct goods or services as a separate promise was included in paragraph 23.17 of the Exposure Draft instead of in the definition of a promise. This was done to simplify the proposed definition of a promise.

***Feedback received***

68. Some respondents (mostly accounting firms and accounting bodies) who commented on Section 23 of the Exposure Draft said the term ‘performance obligation’ should be used in the section instead of ‘promise’ (that is, the terminology should not be simplified). Many of these responses said using the term ‘promise’ in Section 23 would be confusing for preparers and users familiar with IFRS 15.

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69. The fieldwork on the proposed revised Section 23 focused on the judgements that an SME would be required to make when applying the Section and not specific simplifications. Most participants were able to identify the promises in a contract. Participants were not asked if they found the terminology in the Section understandable. Despite this, one participant said their clients would find the term ‘promise’ more understandable than ‘performance obligation’.

### *Staff analysis*

70. The respondents’ concerns about the term ‘promise’ focus on difficulties that may be experienced by users and preparers familiar with IFRS 15.
71. The simplified terminology is not expected to affect the information in SMEs’ financial statements. Therefore, the staff think the simplified terminology would not affect users’ understanding of SMEs’ revenue from contracts with customers.
72. Preparers familiar with IFRS 15 are not believed to be typical of those applying the *IFRS for SMEs* Accounting Standard. This means any difficulties would affect a minority of preparers of SMEs’ financial statements.
73. Respondents did not provide any examples of difficulties that may be experienced by users and preparers familiar with IFRS 15 because of the simplified terminology. No difficulties were identified by participants in the fieldwork on Section 23 who were familiar with IFRS 15.
74. The SMEIG discussed the simplified terminology when it met in July 2023. The number of SMEIG members who thought the terminology should be simplified was comparable to the number who thought the terminology should not be simplified. SMEIG members identified some difficulties that may arise because of the simplified terminology. These are discussed in paragraphs 75–84 of this paper.

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***Assessing the effect of the proposed simplification***

75. Practitioners familiar with IFRS 15 may assess the effect of the simplifications to the requirements of IFRS 15 when applying the revised Section 23. This would involve analysing whether an entity would reach a different outcome if the entity applied the revised Section 23 compared with IFRS 15. Assessing the effect of simplified terminology would be more challenging than assessing the effect of other simplifications proposed to the requirements of IFRS 15.
76. Replacing the term ‘performance obligation’ with ‘promise’ is not intended to change the outcome reached by an entity when identifying goods or services in a contract that should be accounted for separately. This is because an entity identifies what goods or services should be accounted for separately based on whether the goods or services are distinct. Replacing the term ‘performance obligation’ with ‘promise’ does not directly change the requirements for determining if a good or service is distinct.
77. Simplifications were made to the requirements in IFRS 15 for determining if a good or service is distinct in the proposed revised Section.<sup>22</sup> These proposed simplifications may change the outcome of the requirements compared to IFRS 15. Using the term ‘promise’ changes the appearance of the requirements for determining if a good or service is distinct, but does not change the principle of these requirements. Therefore, simplified terminology results in only a cosmetic change to IFRS 15.
78. Explaining the intended effect of using the term ‘promise’ in the Basis for Conclusion to the *IFRS for SMEs* Accounting Standard could overcome the difficulties for practitioners of assessing the effect of the simplified terminology. The explanation could be based on the staff analysis in paragraphs 76–77 of this paper.

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<sup>22</sup> These simplifications are summarised in Question 8 of the [Invitation to Comment in the Exposure Draft Third edition of the IFRS for SMEs Accounting Standard](#).

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***Distinguishing whether a promise is distinct***

79. Practitioners often say that to identify the performance obligations in a contract, IFRS 15 requires entities to determine whether a promise is distinct. This suggests that a promise that is distinct is a performance obligation (that is, a distinct promise is a performance obligation). Based on this description, replacing the term ‘performance obligation’ with ‘promise’ would confuse the distinction between:
- (a) a promise that is not distinct and is not accounted for separately; and
  - (b) a promise that is distinct and is accounted for separately as a performance obligation.
80. The requirements in IFRS 15 for identifying performance obligations in a contract are based on whether the goods or services promised to a customer are distinct. The principle of distinct applies to goods and services, not promises. The confusion described in paragraph 79 of this paper is a consequence of practitioners misinterpreting how the principle of distinct applies. Although using the term ‘promise’ may create confusion in scenarios where the principle is misinterpreted, the term does not cause or contribute to this misinterpretation.
81. The IASB have decided to reflect the principles of IFRS 15 in the *IFRS for SMEs* Accounting Standard. Consequently, the staff do not think the IASB should avoid simplifying the terminology in the *IFRS for SMEs* Accounting Standard because doing so potentially conflicts with a misinterpretation of IFRS 15.

***Reduced applicability of guidance on IFRS 15***

82. Using different language in the revised Section 23 for key terms in IFRS 15 makes it difficult for practitioners to refer to guidance on IFRS 15 issued by the IASB and others when implementing Section 23.
83. The *IFRS for SMEs* Accounting Standard is intended to be a stand-alone document. SMEs are expected to be able to apply the Standard without having to refer to material outside the Standard. Although referring to guidance on IFRS 15 may be helpful for



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SMEs, doing so should not be necessary for SMEs to understand the requirements in the revised Section 23. Creating an impression that referring to such guidance is necessary places an additional burden on SMEs to familiarise themselves with the guidance on IFRS 15.

84. The requirements for identifying performance obligations in IFRS 15 are different compared with the proposed requirements for identifying promises in the revised Section 23 (as discussed in paragraph 77 of this paper). Therefore, there are instances when it would be inappropriate for SMEs to refer to guidance on IFRS 15 about identifying performance obligation. For example, an SME and an entity applying IFRS 15 might reach different outcomes because changes have been made to the requirements proposed in the revised Section 23 for:
- (a) determining whether a good or service is distinct;
  - (b) accounting for warranties (see paragraph BC191(d) of the Exposure Draft);  
and
  - (c) accounting for customer options for additional goods or services (see paragraphs 24–44 of this paper).
85. In addition to the difficulties identified by SMEIG members, the PIR of IFRS 15 found that most entities took time to understand the terminology used in IFRS 15.<sup>23</sup> SMEs are expected to spend less time learning and familiarising themselves with new accounting terminology compared with entities applying full IFRS Accounting Standards. Consequently, it is likely to take longer for SMEs to understand the terminology in the revised Section 23 compared with the time taken for entities to understand the terminology in IFRS 15. Using simpler and more accessible terminology for key terms in the revised Section 23 would reduce the initial challenge for SMEs of adapting to the terminology and help to shorten the time taken for SMEs to understand it.

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<sup>23</sup> Spotlight 1 of [Request for Information Post-implementation Review of IFRS 15 Revenue from Contracts with Customers](#).

86. The feedback on the simplified terminology focuses on potential difficulties relevant to a minority of practitioners applying the *IFRS for SMEs* Accounting Standard. The staff think the costs created by these difficulties do not outweigh the benefits of the simplified terminology. Therefore, the staff recommend the term ‘promise’ is used in the revised Section 23, instead of the term ‘performance obligation’.

#### Question for the IASB

4. Does the IASB agree to use the term ‘promise’ in the revised Section 23, instead of the term ‘performance obligation’?

### ***Measuring variable consideration***

87. IFRS 15 includes requirements for determining the transaction price in a contract if the consideration includes a variable amount. An amount of consideration can vary because of discounts, penalties, performance bonuses and other similar items. Entities determine the amount of variable consideration to include in the transaction price by:
- (a) estimating the amount of consideration that the entity expects to be entitled to; and
  - (b) constraining the estimate of variable consideration in (a).<sup>24</sup>
88. The Exposure Draft proposed requirements similar to those described in paragraph 87 of this paper.<sup>25</sup> However, the expression of the requirement in IFRS 15 to constrain estimates of variable consideration was simplified. In the Exposure Draft, the requirement to constrain estimates was reframed in the positive by focusing on consideration that will become due instead of revenue reversals that will not occur.<sup>26</sup>

<sup>24</sup> Paragraphs 50 and 56 of IFRS 15.

<sup>25</sup> Paragraphs 23.43–23.47 of the Exposure Draft.

<sup>26</sup> Paragraph 56 of IFRS 15 requires estimates of variable consideration to be included in the transaction price ‘only to the extent that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur when the uncertainty associated with the variable consideration is subsequently resolved’. Paragraph 23.46 of the Exposure Draft requires estimates of variable consideration to be included in the transaction price ‘only to the extent that it is highly probable that this amount will become due when the uncertainty associated with the variable consideration is subsequently resolved’.

The confidence level that an estimate of variable consideration must pass before it can be included the transaction price was the same as IFRS 15 (that is, ‘highly probable’).

### *Feedback received*

89. Some respondents (mostly accounting firms and accounting bodies) who commented on Section 23 of the Exposure Draft said the requirement to constrain estimates of variable consideration should not be simplified (that is, the requirement should be the same as IFRS 15). Most of these respondents were concerned that the amount of variable consideration recognised by an SME would be different to the amount of variable consideration recognised by an entity applying IFRS 15.
90. Most fieldwork participants who were unfamiliar with IFRS 15 were unable to make the judgements required to determine the amount of variable consideration. Some of these participants said determining the amount of variable consideration is difficult because it involves significant judgement and complex calculations. A few participants said SMEs should determine the amount of variable consideration based on the actual amount of consideration received (or receivable) instead of an estimate.

### *Staff analysis*

#### ***Constraining estimates of variable consideration***

91. The expression of the requirement to constrain estimates of variable consideration in IFRS 15 was simplified in the Exposure Draft to make the requirement easier for SMEs to understand and apply. By using different language to express the requirement, SMEs may not get to the same outcome as entities applying IFRS 15. If the outcome is different, SMEs are still expected to determine an amount of variable consideration that faithfully depicts the amount of consideration to which the SME is entitled. Consequently, the staff think that making the requirement easier to understand and apply should be prioritised ahead of making the outcome the same as IFRS 15. Therefore, the staff recommend the simplified expression of the requirement is retained in the revised Section 23.

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***Applying hindsight***

92. Requiring SMEs to determine the amount of variable consideration based on the actual amount of consideration received (or receivable) would result in SMEs applying hindsight. Hindsight would reduce the judgement needed to measure variable consideration and provide users of financial statements with more reliable information about SMEs' revenue. However, allowing SMEs to apply hindsight is inconsistent with other requirements in the proposed Section 23 and the *IFRS for SMEs* Accounting Standard which require SMEs to make judgements based on conditions that existed at the end of the reporting period.
93. As an example, the proposed revised Section 23 requires SMEs to measure the progress of promises to transfer goods or services that are satisfied over time. Measuring progress requires SMEs to make estimates. An SME must estimate:
- (a) the total goods or services to be transferred under the contract, if the SME measures progress using an output method; or
  - (b) the total expected inputs needed to satisfy the promise, if the SME measures progress using an input method.<sup>27</sup>
94. In contracts where the amount of consideration varies, the amounts in paragraph 93(a)–(b) of this paper may also vary because of the same uncertainty associated with the variable consideration. An SME would need to estimate the variable consideration and the amounts in paragraph 93(a)–(b) when accounting for such contracts. The SME would apply hindsight to estimate the amount of variable consideration, but not when estimating the other amounts. This mixed approach to applying hindsight might be confusing for preparers and users.
95. The inconsistencies created by requiring SMEs to apply hindsight could be overcome by allowing hindsight to be applied in other areas of the revised Section 23 and the *IFRS for SMEs* Accounting Standard. However, doing so undermines the general

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<sup>27</sup> Paragraph 23.91 of the Exposure Draft.

requirement for financial statement to provide information about conditions that exist at the end of the reporting period. Introducing exceptions to this requirement also makes the Standard more complex. Consequently, the staff do not recommend that SMEs apply hindsight to measure variable consideration.

***Timing of revenue recognition***

96. Requiring SMEs to determine the amount of variable consideration based on the actual amount of consideration received (or receivable) would result in SMEs recognising variable consideration only if the amount of variable consideration received (or receivable) is known. An SME would recognise variable consideration only if the uncertainty associated with the consideration was resolved by the date the SME's financial statements were authorised for issue. If the uncertainty associated with the variable consideration was not resolved by this date, the SME would recognise no variable consideration. The SME would instead recognise the variable consideration in a later reporting period, which may be after the related goods or services have been transferred to the customer.
97. A core principle of the revenue recognition model in IFRS 15 is that an entity should recognise revenue to depict the transfer of goods or services to a customer. Requiring SMEs to recognise variable consideration only if the amount of variable consideration received (or receivable) is known conflicts with this principle. Consequently, the staff do not recommend that SMEs recognise variable consideration only if the amount of variable consideration received (or receivable) is known.

***Challenges for preparers***

98. Some fieldwork participants who were unfamiliar with IFRS 15 said determining the amount of variable consideration would be difficult because it involves significant judgement and complex calculations.
99. Feedback on determining variable consideration was received as part of the PIR of IFRS 15. Some respondents to the Request for Information reported challenges related

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to determining variable consideration. These challenges arose in specific circumstances, not all circumstances.<sup>28</sup>

100. Similar to the challenges experienced by entities applying IFRS 15, the difficulties identified by the fieldwork participants are expected to arise when SMEs account for certain types of contracts, not all contracts. For example, SMEs are expected to make significant judgments and perform complex calculations if determining the amount of variable consideration in long-term contracts where goods or services are specific to each customer (for example, a construction contract). However, most SMEs are expected to have simple contracts and are not expected to encounter these difficulties.
101. Fieldwork participants also said that a common cause of variable consideration in contracts between SMEs and their customers is prompt payment discounts. Determining the variable consideration in contracts that include such discounts should be straightforward.
102. SMEs that have more complex contracts may encounter challenges when determining variable consideration. The staff think these challenges would be overcome as SMEs become familiar with the requirements for measuring variable consideration in the revised Section 23. Educational material on the revised Section 23 would also help SMEs apply the requirement to more complex contracts. The staff do not think further simplifications are needed to the requirements in the Exposure Draft for this subset of SMEs and contracts. Consequently, the staff recommend the requirements proposed in the Exposure Draft for measuring variable consideration are retained in the revised Section 23.

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<sup>28</sup> Paragraphs 30–31 of [Agenda Paper 6A Feedback summary—IFRS 15 requirements](#) of the January 2024 IASB meeting.

103. The SMEIG discussed the requirements for measuring variable consideration at its meetings in July and December 2023. SMEIG members generally agreed with the staff recommendations to retain:
- (a) the requirements in the Exposure Draft for measuring variable consideration in the revised Section 23; and
  - (b) the simplified expression of the requirement in IFRS 15 to constrain estimates of variable consideration in the revised Section 23.
104. SMEIG members also generally agreed with the staff recommendation not to allow SMEs to determine the amount of variable consideration based on the actual amount of consideration received (or receivable).

Question for the IASB

5. Does the IASB agree to retain the requirements proposed in the Exposure Draft for measuring variable consideration in the revised Section 23?

***Measuring non-cash consideration***

105. The Exposure Draft proposed requirements for determining the transaction price for contracts in which a customer promises consideration in a form other than cash (non-cash consideration). Under these proposals, SMEs would be required to measure non-cash consideration at fair value. However, if an SME cannot reasonably estimate the fair value of non-cash consideration, the consideration would be measured indirectly by reference to the stand-alone selling price of the goods or services promised to the customer in exchange for the consideration.<sup>29</sup>
106. The requirements proposed for non-cash consideration in the Exposure Draft are aligned with the requirements in IFRS 15.<sup>30</sup>

<sup>29</sup> Paragraph 23.60 of the Exposure Draft.

<sup>30</sup> Paragraphs 66–69 of IFRS 15.

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*Feedback received*

107. Among fieldwork participants unfamiliar with IFRS 15, there were comparable numbers who were able to measure non-cash consideration and who were not. Of the participants who were unable to measure non-cash consideration, there were equal numbers who:
- (a) were unsure which transactions are in scope of the proposed requirements for non-cash consideration; and
  - (b) were unable to measure non-cash consideration because it involves significant judgement.
108. Transactions that fieldwork participants thought were in scope of the proposed requirements were:
- (a) transactions addressed by other requirements in the proposed revised Section 23 (for example, non-monetary exchanges between entities in the same line of business to facilitate sales to customers or potential customers, which is addressed in paragraph 23.1(d) of the Exposure Draft); and
  - (b) transactions when an SME receives cash (for example, cash received via an electronic transfer system).

*Staff analysis****Scope of the proposed requirements***

109. The fieldwork participants' responses were based on an initial study of the proposed revised Section 23. Additionally, only a few participants said their clients commonly receive non-cash consideration. Therefore, participants were commenting on requirements that they had not applied and would generally not apply. For these reasons, the staff think that any initial difficulties of understanding the scope of the proposed requirements for non-cash consideration would be overcome as SMEs become familiar with the requirements in the revised Section 23.



110. Entities typically receive non-cash consideration if they enter into barter transactions (that is, exchanges of dissimilar goods or services). To help SMEs identify transactions that may be in scope of the requirement proposed for non-cash consideration, the staff recommend the term ‘barter’ is included in the description of non-cash consideration in the revised Section 23.

***Level of judgement***

111. The fieldwork participants’ comments on the judgement involved in measuring non-cash consideration focused on the proposed requirement to estimate the fair value of the consideration (the inbound asset).

112. Paragraph 23.60 of the Exposure Draft proposed that if the SMEs cannot reasonably estimate the fair value of the inbound asset, SMEs measure the inbound asset by reference to the stand-alone selling price of the goods or services being transferred to the customer (the outbound asset).

113. The feedback suggests that fieldwork participants unfamiliar with IFRS 15 overlooked the exemption from measuring the fair value of the inbound asset proposed in paragraph 23.60 of the Exposure Draft. This may be because exemptions from requirements to measure items at fair value are typically included as undue cost or effort exemptions in the *IFRS for SMEs* Accounting Standard. To avoid preparers overlooking the exemption, the staff recommend presenting separately in the revised Section 23:

- (a) the requirement to measure the fair value of non-cash consideration; and
- (b) the exemption from the requirement to measure the fair value of non-cash consideration.

114. The SMEIG considered the staff recommendations in paragraphs 110 and 113 of this paper when it met in December 2023. SMEG members generally agreed with the recommendations.

#### Question for the IASB

6. Does the IASB agree:
- a. to include the term 'barter' in the description of non-cash consideration in the revised Section 23; and
  - b. to present separately in the revised Section 23:
    - i. the requirement to measure the fair value of non-cash consideration; and
    - ii. the exemption from the requirement to measure the fair value of non-cash consideration?

#### ***Allocation based on stand-alone selling prices***

115. The Exposure Draft proposed requiring SME to allocate the transaction price to each promise identified in a contract on a relative standalone selling price basis.<sup>31</sup> Under this proposal, an SME must identify the standalone selling price of the good or service underlying each promise in the contract. If the standalone selling price of a good or service is not directly observable, an SME must estimate it.<sup>32</sup> Paragraph 23.66 of the Exposure Draft described three suitable methods for estimating the standalone selling price.
116. The requirements proposed for allocating the transaction price in the Exposure Draft are aligned with the requirements in IFRS 15.<sup>33</sup>

#### ***Feedback received***

117. Among fieldwork participants unfamiliar with IFRS 15, there were comparable numbers who were able to allocate the transaction price to the promises in a contract and who were not.

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<sup>31</sup> Paragraph 23.63 of the Exposure Draft.

<sup>32</sup> Paragraph 23.65 of the Exposure Draft.

<sup>33</sup> Paragraphs 76–80 of IFRS 15.

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118. A few participants suggested restricting the instances when an SME is required to allocate the transaction price to the promises in the contract, for example, not requiring allocation if the contract is less than 12 months. One participant said that compared with entities that apply IFRS 15, SMEs are less likely to sell goods and services separately that are usually sold together. Consequently, SMEs are more likely to estimate standalone selling prices because the prices are not directly observable.
119. A few respondents (mostly accounting bodies) who commented on Section 23 of the Exposure Draft said the IASB should simplify the proposed requirements for allocating the transaction price.

#### *Staff analysis*

120. Half of the fieldwork participants who were unfamiliar with IFRS 15 were not able to allocate the transaction price to the promises in a contract. However, when the proposed requirements for allocating the transaction price were explained to the participants interviewed, the requirements were often considered straightforward and logical in the context of the revenue recognition model.
121. Most SMEs are expected to have simple contracts. Consequently, the proposed requirements for allocating the transaction price are expected to be straightforward to apply for most contracts. If the standalone selling price of a good or service must be estimated, the estimate is expected to be an intuitive judgement that SMEs can make without having to consider a large amount of information. The Exposure Draft described suitable methods for estimating standalone selling prices, however, it is expected that most SMEs would be able to make the estimate without having to refer to this guidance.
122. The staff think the guidance on methods for estimating standalone selling prices overcomplicates the requirements in this area. The guidance hinders SMEs' understanding of the requirements by making them appear unduly complex. To avoid overcomplicating the requirements, the staff recommend the guidance is included in

separate educational material instead of in the revised Section 23. By doing so, the guidance can be referred by SMEs that are accounting for more complex contracts.

123. Including the guidance on estimating standalone selling prices in separate educational material would mean the revised Section 23 would include less guidance on this estimate compared with IFRS 15. This is consistent with other accounting estimates, where the *IFRS for SMEs* Accounting Standard includes less guidance on estimation techniques compared with full IFRS Accounting Standards (for example, guidance on measuring the fair value of equity instruments or the cost of inventories). The *IFRS for SMEs* Accounting Standard includes less guidance on these estimates because SMEs typically have simpler transactions compared with entities applying full IFRS Accounting Standards.
124. The staff recommendation in paragraph 122 of this paper is a more appropriate way to simplify the requirements for allocating the transaction than the suggestion made by fieldwork participants to introduce an exemption from the requirements described in paragraph 118 of this paper. The suggestion would exempt SMEs from accounting for goods or services separately, which would undermine the principle of IFRS 15.
125. The SMEIG considered the staff recommendation in paragraph 122 of this paper when it met in December 2023. SMEIG members generally agreed with the recommendation.

#### Question for the IASB

7. Does the IASB agree to include the guidance on methods for estimating standalone selling prices in separate educational material instead of in the revised Section 23?

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***Allocating variable consideration***

126. IFRS 15 includes criteria that specify circumstances when an entity is required to allocate variable consideration entirely to one or more, but not all, performance obligations in a contract.<sup>34</sup> Only in these circumstances is the entity required to depart from allocating variable consideration on a relative stand-alone selling price basis (the default method).
127. The Exposure Draft proposed requirements for SMEs to depart from allocating variable consideration using the default method. Under the proposals, an SME is required to use an alternative method if the default method does not depict the amount of consideration to which the SME expects to be entitled in exchange for transferring the goods or services.<sup>35</sup> The proposed requirements for allocating variable consideration in the Exposure Draft are the same as the proposed requirements for allocating discounts.<sup>36</sup>

***Feedback received***

128. Most fieldwork participants who were unfamiliar with IFRS 15 were unable to allocate variable consideration to the promises in a contract. Some participants said the information needed to make the judgement would be difficult to obtain. This was because the terms for variable consideration are often approved by oral agreement and not documented. One participant said that SMEs typically negotiate different terms for different customers.
129. Some fieldwork participants said it would be difficult to decide whether:
- (a) a contract includes variable consideration (and the proposed requirements for allocating variable consideration apply); or

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<sup>34</sup> Paragraph 85 of IFRS 15.

<sup>35</sup> Paragraph 23.70 of the Exposure Draft.

<sup>36</sup> Paragraphs 23.68–23.69 of the Exposure Draft

- (b) a customer has received a discount (and the proposed requirements for allocating a discount apply).

This is because variable consideration can arise because of a discount offered by the SME (for example, a cumulative quantity discount).

### *Staff analysis*

#### ***Information needed to make the judgement***

130. The requirements proposed in the Exposure Draft require an SME to assess if allocating variable consideration using the default method depicts the amount of consideration to which the SME expects to be entitled in exchange for transferring the goods or services. To do so, the SME must decide whether the variable consideration is attributable to the entire contract, or to specific parts of the contract.
131. Feedback from fieldwork participants indicates that SMEs commonly negotiate and agree variable consideration terms with their customers verbally. As a result, terms may not be documented and may differ between contracts.
132. In instances when the variable consideration terms are not documented, SMEs are expected to negotiate the terms for the overall contract, instead of for specific goods or services promised in the contract (that is, the terms would be negotiated as a package). This is because assessing the effect of changing the terms of the entire contract is easier than assessing the effect of changing the terms for specific goods or services. For example, if an SME agrees a volume discount with their customer, it is easier to assess the effect of changing the discount for the entire contract instead of for specific items in the contract. Consequently, the variable consideration would be expected to be attributable to the entire contract.
133. Instances may also occur when the variable consideration terms are not documented, and an SME negotiates the terms based on the specific goods or services promised to the customer. For example, if an SME agrees a volume discount with their customer, the discount may be based on the number of high-margin items sold, instead of the

value of the entire contract. In such instances, the variable consideration would be attributable to specific parts of the contract.

134. Based on the analysis in paragraphs 132–133 of this paper, an SME’s approach to negotiating variable consideration terms is likely to determine whether the variable consideration is attributable to the entire contract, or to specific parts of the contract. Changes in variable consideration terms can have a significant effect on the overall profitability of a contract. Consequently, SMEs are expected to know how variable consideration terms are negotiated, even if the terms are not documented. SMEs are also expected to take a consistent approach to negotiating contracts, even if the terms agreed are different. Therefore, SMEs would be able to determine if allocating variable consideration using the default method is appropriate in instances where the variable consideration terms are not documented and differ between customers.

***Differentiating between variable consideration and discounts***

135. When allocating variable consideration and discounts to promises in a contract, it is unnecessary for SMEs to differentiate between these amounts because the proposed requirements for allocating these amounts are the same. Therefore, the staff recommend combining the requirements for allocating variable consideration and discounts in the revised Section 23.
136. The SMEIG considered the staff recommendation in paragraph 135 of this paper when it met in December 2023. SMEIG members generally agreed with the recommendation.

Question for the IASB

8. Does the IASB agree to combine the requirements for allocating variable consideration and discounts together in the revised Section 23?

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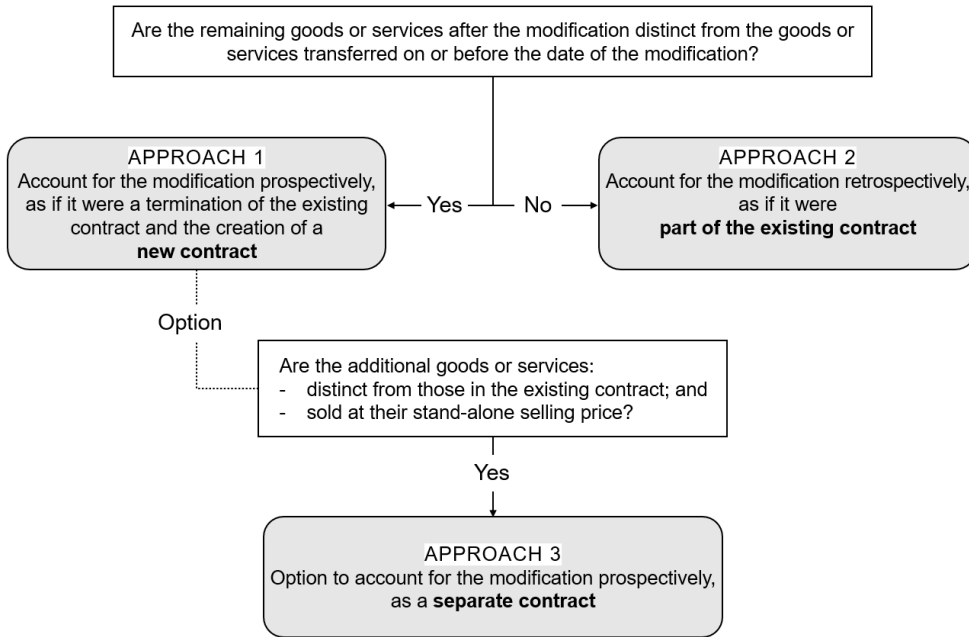
## **Next steps**

137. The staff will bring papers to the IASB on:
- (a) the remaining seven topics where stakeholders requested changes to, or raised concerns about, the requirements proposed in the Exposure Draft;
  - (b) additional and alternative simplifications to the requirements in IFRS 15 suggested by stakeholders; and
  - (c) changes to the structure and language of Section 23 of the Exposure Draft.



**Appendix—Figures illustrating the recommended change to the proposed requirements for contract modifications**

**Figure 1—Summary of the requirements for contract modifications proposed in the Exposure Draft**



**Figure 2—Summary of the requirements for contract modifications as a consequence of the staff recommendation**

