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Variable consideration
Cover Note

Objective

1 Based on previous discussions of EFRAG TEG, the purpose of this session is to:

(a) Discuss an interpretation/approach to recognise an equity component when a variable consideration to be settled by transferring a financial instrument depends on the purchaser's future actions, and decide whether to consider this approach further/in the Discussion Paper;

(b) Consider a 'mapping' of current requirements on variable consideration and discuss whether some of the current differences in accounting for variable consideration result in the most useful information;

(c) Consider the revised structure of EFRAG's Discussion Paper.

Background

2 The issues to be considered in this session result from previous discussions of EFRAG TEG. The table below lists the comments made by EFRAG TEG at the July 2021 and September 2021 EFRAG TEG meetings and when/how these are planned to be addressed.

Comments	Actions
At the July 2021 EFRAG TEG meeting, TEG members confirmed that there were different interpretations on how to account for variable consideration that was within the control of the purchaser.	EFRAG TEG's conversation confirmed that there are two issues related to variable consideration: 1) Lack of (clear) guidance for some types of variable consideration; and 2) Different guidance for other types of variable consideration. EFRAG TEG agreed that both these issues should be considered for the Discussion Paper. EFRAG TEG will be asked, at a future meeting, whether this issue should be considered, for example by developing an approach to ensure consistency among the different guidance or whether EFRAG TEG considers that there are valid reasons for having different guidance (and therefore not develop a consistent approach).
When examples of variable consideration were considered at the July 2021 EFRAG TEG meeting, it was mentioned that in some cases, where the variability would depend on the purchaser's future actions, it	This issue is to be considered in this session – Agenda Paper 10-02.

could be argued that before those future actions would take place, the purchaser could have an equity component that would then become a liability when the entity would start using the intangible asset.	
At the July 2021 EFRAG TEG meeting, it was decided that the notion of 'cost' in IFRS should be considered.	The notion of 'cost' was discussed at the September 2021 meeting. In that regard, the following comments were made, which will be taken into consideration when drafting the Discussion Paper (Refer to Agenda Paper 10-04 for the Structure of EFRAG's Discussion Paper): • EFRAG TEG generally agreed that there could be different interpretations on 'cost' as concluded in Agenda Paper 06-04 for the September 2021 meeting. • EFRAG TEG agreed that changes in variable consideration related to the period before an asset covered by IAS 16 *Property, Plant and Equipment* or IAS 38 *Intangible Assets* would be ready for its intended use should be included in the cost of the asset. • It was noted that the notion of 'cost' in the IASB ED *Regulatory Assets and Regulatory Liabilities* should also be considered as it could reflect the IASB's latest thinking and suggested that cost could be updated. • The discussion on 'cost' should also include how 'cost' is defined in the Conceptual Framework. • It was noted that the terminology used in the Agenda Paper for the September 2021 EFRAG TEG meeting should be considered.
At the July 2021 EFRAG TEG meeting, the view was expressed that the Discussion Paper should not consider an approach based the notion of expectation as such an approach would not be compatible with the Conceptual Framework which, among other things, focuses on the practical ability to avoid.	An approach based on what the entity expects to do will not be considered in the Discussion Paper.
At the July 2021 EFRAG TEG meeting, it was decided that it should be further considered whether the Conceptual Framework could provide guidance on when to recognise a liability. In this regard it should be considered what 'no practical ability to avoid' in the Conceptual Framework could mean in the case where an asset had been acquired, but an additional consideration had to be paid to use the asset. The view was presented that in such a case, the entity would not have a practical ability to avoid (unless the entity	The guidance on when to recognise a liability was considered at the September 2021 EFRAG TEG meeting. In that regard, the following comments were made to the agenda paper prepared by the EFRAG Secretariat, which will be taken into consideration when drafting the Discussion Paper: • The Conceptual Framework is not clear with regards to the role of economic

did not intend to use the asset – e.g. because it would just keep competitors from using it). It should also be considered what should be 'the past event': the transfer of the asset or the action of the purchaser that trigger the payment (or both). In this regard the IASB's conclusions on the regulatory asset and liability project could be considered. In this project, it seemed that the IASB considered that if you had two possible 'past events' it was the first event that should be taken into account.	compulsion when considering 'no practical ability to avoid'. • There are differing views on whether the 'past event' would always be when the purchaser would obtain control of a good or service. It could be argued that sometimes the purchaser would not have economic benefits from receiving an asset, but only when it started using an asset received (e.g. if the asset should deliver some specified performance targets). • The establishment of the contract should not be considered as the past event. IFRS 16 *Leases* states that the past event is when an asset is received – not when a contract is established. • The Discussion Paper should have a discussion on the Conceptual Framework without reaching a conclusion on the issues mentioned above. • If it would be included in the Discussion Paper, better arguments should be provided when stating that an entity would have no practical ability to avoid a reduction in sales or not using an acquired asset. • The discussion should consider constructive obligations (for example, restructuring costs under IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*). • The discussion on executory contracts should be extended.
At the July 2021 EFRAG TEG meeting, it was mentioned that it should be considered whether the manner the purchaser of an asset for variable consideration should account for the transaction could be based on how the seller would account for it.	An 'IFRS 15 (*Revenue from Contracts with Customers)* mirroring approach' is to be considered in this session in Agenda Paper 10-03.
At the July 2021 EFRAG TEG meeting, it was mentioned that it should be considered whether IFRS 16 would be a good candidate for an approach for recognition of a liability for variable consideration as its requirements on variable consideration were not based on conceptual arguments.	The EFRAG Secretariat will reflect the Basis for Conclusions related to IFRS 16 in the Discussion Paper. The EFRAG Secretariat currently plans to mention IFRS 16 and its requirements in the Discussion Paper. EFRAG TEG can consider at a later stage whether any mentioning of IFRS 16 should be removed from the Discussion Paper.
At the July 2021 EFRAG TEG meeting, EFRAG TEG agreed that if the variability related to variable consideration is outside the control of the purchaser, a liability for	In the Discussion Paper, the description of the issue on the lack of (clear) guidance on when to recognise a liability for variable consideration will be limited to the

variable consideration should be recognised.	situations where the variability is dependent on the purchaser's future actions.
It should be kept in mind that although no liability would be recognised, there could still be direct costs related to acquiring an asset, that should be capitalised.	The EFRAG Secretariat will consider whether it would be relevant to mention this in the Discussion Paper. When considering the Discussion Paper, EFRAG TEG is encouraged to note if this comment has not been appropriately reflected.
At the July 2021 EFRAG TEG meeting, EFRAG TEG members agreed that in a contract containing both a fixed payment and a variable payment, recognition of a liability related to the variable part should be considered independently.	The Discussion Paper will include this premises for its discussion in a subsection on the unit of account.
At the July 2021 EFRAG TEG meeting, it was noted that as it could be discussed whether a liability to pay with bitcoins would fall under IAS 37, an example including Bitcoins should not be included in the Discussion Paper.	The Discussion Paper will not include an example with payment with Bitcoins.
At the September 2021 EFRAG TEG meeting, in relation to the question on whether differences in existing guidance should be assessed, EFRAG TEG agreed to discuss in the Discussion Paper why the guidance on variable consideration in current IFRS Standards is different and "map" the different guidance without trying to identify an approach that should be applied in all cases.	A paper on this has been prepared for this session – Agenda Paper 10-03.
At the September 2021 EFRAG TEG meeting, it was noted that in the discussions it was important to take into account what would drive the variability and the nature of the liability. For example, whether it would relate to the value of the asset or not.	This comment is reflected in Paper 10-03 for this session.
At the September 2021 EFRAG TEG meeting, it was noted that another issue that should be discussed would be whether, in some cases, the seller retains an interest in an asset transferred. This could either be limited or unlimited in time. If it was limited in time, it could be considered whether this was similar to an acquisition made in steps. If it would be unlimited, it was a question on whether you had acquired the entire asset or not. It could then also be questioned whether this was related to the characteristics of the asset, and it could be considered as an argument for updating cost even when a liability would not be recognised initially.	This issue will be discussed at a forthcoming meeting. At a forthcoming meeting, EFRAG TEG will also discuss whether/how the Discussion Paper should consider risk-sharing arrangements.
At the September 2021 EFRAG TEG meeting, an approach to account for	These approaches are considered in Paper 10-03 for this session.

variable consideration (which is not directly reflected in any current IFRS Standards) was suggested. Under the approach, a liability for variable consideration would be recognised and changes would be reflected in cost to the extent the variability would relate to the quality/value of the asset. In other cases, a liability should not initially be recognised and subsequent changes should be included in profit or loss. Two variations of this approach were also mentioned: • Not to recognise any liability when control of the asset would be transferred as a 'past event' could be argued only to occur when the quality of the asset would subsequently be determined. Until then, it was uncertain whether the seller had transferred what was promised. • Recognise a liability in both cases, but only reflect subsequent changes in the cost to the extent the changes related to the value of the asset (and not, for example, the use of the asset).	

Agenda Papers

3 In addition to this cover note, agenda papers for this session are:

(a) Agenda paper 10-02 – An approach where the purchase may recognise an equity component before a liability is recognised;

(b) Agenda paper 10-03 – Mapping of recognition and measurement of variable consideration in existing IFRS Standards; and

(c) Agenda paper 10-04 – Revised structure of the Discussion Paper.