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25 YEARS OF
PROFESSIONAL
EXCELLENCE

IFRS 15

Revenue from Contracts with Customers

- CA Joseph Philip.

Introduction

Revenue is income from ‘ordinary activities’.

A **contract** has rights and obligations between two or more parties.

A **customer** receives a good or service.

Issue date

- Issued May 2014.
- Sets out the requirements for recognising revenue that apply to all contracts with customers except for contracts within the scope of;
    - leases,
    - insurance contracts and
    - financial instruments.
- Effective from 1 January 2018.
- Earlier application is permitted.

Supersedes

- IFRS 15 replaces the previous revenue Standards:
  - IAS 18 Revenue
  - IAS 11 Construction Contracts,

- the related Interpretations on revenue recognition:
  - IFRIC 13 Customer Loyalty Programmes,
  - IFRIC 15 Agreements for the Construction of Real Estate,
  - IFRIC 18 Transfers of Assets from Customers and
  - SIC-31 Revenue – Barter Transactions Involving Advertising Services.

Scope exclusions

  - Leases, insurance, financial instruments, certain guarantee contracts and certain non-monetary exchanges
- Contracts with elements in multiple standards
  - Evaluate under other standards first

Brief comparison

IAS 18 /11	*IFRS 15*
Separate models for: • Construction contracts • Goods • Services	**Single model for performance obligations:** • Satisfied over time • Satisfied at a point in time
Focus on risk and rewards	**Focus on control**
Limited guidance on: • Multiple element arrangements • Variable consideration • Licences	**More guidance:** Separating elements, allocating the transaction price, variable consideration, licences, options, repurchase arrangements **and so on….**

Risk & Rewards Vs.Control

- Entity A has an order to deliver goods to a customer overseas. These goods could be shipped on any of the four categories of Incoterms below: • “E”-term (EXW): Entity A only makes goods available to the customer at Entity A’s factory. •.

- “F”-term (FOB): Entity A is required to deliver the goods to a carrier appointed by the customer. • “C”-term (CIF): Entity A contracts for carriage, but without assuming the risk of loss or damage to the goods or additional cost due to events occurring after shipment. • “D”-term (DAF): Entity A bears all costs and risks needed to bring the goods to their destination

- Controll:
- DVD sale with control on resale

Revenue recognition

- Customer acceptance
- Legal title to the customer
- Transfer of risk and rewards
- Supplier has the right to payment
- Transfer of physical possession

Need for change

- Significant diversity in revenue recognition practices
- Limited guidance on many important topics, such as accounting for arrangements with multiple elements.
- Difficult for investors and analysts (‘investors’) to understand and compare a company’s revenue.
- Difficult to apply to complex transactions due to lack of basis for conclusions.
- numerous industry and transaction specific requirements, which often resulted in economically similar transactions being accounted for differently.
- new types of transactions emerges.

Example

- Etisalat mobile sells bundle offer :
- Free handset for one year contract with 500 flexible minutes “ AED 200 pm
- Handset has a standalone price of AED 700
- 500 flexible minures stand alone :AED 140

- Total to pay by customer : AED 2400
- SASP:140x 12 = 1680+700 =2380
- PO SASP TP Revenue

1) FM 1680 1694 141

2) Handset 700 706 706

1680/2380 2380 2400

- Handset to recognize immediately :706
- FM :1694/12 = 141 revenue
- Difference = 200-141 = 59/-
- Journal Entry:
- Contract Asset 706
- To Revenue 706

DR - COS CR inventory

- AR Dr: 200
- Revenue 141
- Contractual asset 59

The framework five steps

Identify the contract(s) with the customer

Identify the performance obligations in the contract

Determine the transaction price

Allocate the transaction price

Recognise revenue when a performance obligation is satisfied

Order of application

Core principle

Revenue recognised to depict transfer of goods or services

Step 1 - Identify the contract with the customer

Step 2 - Identify the performance obligations in the contract

Step 3 - Determine the transaction price

Step 4 - Allocate the transaction price

Step 5 - Recognise revenue when (or as) a performance obligation is satisfied

Step 1

- Agreement between two or more parties that creates enforceable rights and obligations
- No contract unless customer committed, criteria include:
  - it is probable that the entity will collect the consideration to which it will be entitled
- Combine two or more contracts with the same customer when:
  - negotiated as a package with a single commercial objective;
  - amount of consideration to be paid in one contract depends on the price or performance of the other contract; or
- goods or services promised in the contracts are a single performance obligation (see step 2)

Step 2: Performance obligation

- Performance obligations are promises to transfer goods or services to a customer that are:
  - explicit,
  - implicit, or
- arise from customary business practices
- Identifying performance obligations is critical to measurement and timing of recognition

Step 3 transaction price

- Probability weighted or best estimate
- More specific guidance covering:
  - time value of money
  - constraint on variable consideration
  - non-cash consideration
- consideration payable to customers: reduction to transaction price unless for a distinct good or service.

Step 4: Allocation of price

- Allocate transaction price to separate performance obligations based on relative standalone selling price:
- Actual or estimated
- Residual ‘approach’ if selling price is highly variable or uncertain (change from current practice)
- Initial allocation and changes to variable consideration might be allocated to a single performance obligation if:
- Contingent payment relates only to satisfaction of that performance obligation, and
- Allocation is consistent with the amount the entity expects to be entitled to for that performance obligation

Step 5: Revenue recognition

- Guidance applies to each separate performance obligation
- First, evaluate if performance obligation satisfied ‘over time’
- recognise revenue based on the pattern of transfer to the customer

- If not point in time
- recognise revenue when control transfers

Transaction cost

- Incremental costs of obtaining a contract required to be capitalised if expected to be recovered (e.g. sales commissions)
- May be expensed if expected contract period less than 1 year
- Contract fulfilment costs
- Look to other guidance first (inventory, PPE)
- If out of scope of other standards, required to be capitalised if:
- Relate directly to a contract and
- Relate to future performance and
- Expected to be recovered
- Amortise capitalised costs as control transfers
- Impairment reversals required

Disclosures

- Both qualitative and quantitative information including;
- Disaggregated information
- Contract balances and a description of significant changes
- Amount of revenue related to remaining performance obligations and an explanation of when revenue is expected to be recognised
- Significant judgments and changes in judgments

More implementation guidelines

- Customer options
- Warranties
- Breakage
- Non-cash consideration
- Consideration payable to the customer
- Returns
- Repurchase options
- Principal or agent

- Interactive session
- Question and answers