International Financial Reporting Standards

# Revenue Recognition

The views expressed in this presentation are those of the presenter,
not necessarily those of the IASB or IFRS Foundation

2014 Project update and the future work plan

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# At a glance



- IFRS 15 issued on 28 May 2014
  - Joint Standard with FASB (Topic 606)
  - IFRS 15 replaces IAS 18, IAS 11 and related Interpretations
- Framework for revenue recognition
- Effective date 1/1/2017, early application permitted
- Transition
  - Retrospective or
  - Cumulative effect at the date of application
- Revenue Transition Resource Group

# Extensive due process



2008 | 2010 | 2011 | 2014

**December 2008**

**Discussion Paper**

*Preliminary Views on Revenue Recognition in Contracts with Customers*

*211 comment letters*

**June 2010**

**Exposure Draft**

*Revenue from Contracts with Customers*

*974 comment letters*

*Roundtables*

**November 2011**

**Revised Exposure Draft**

Re-exposure of *Revenue from Contracts with Customers*

*358 comment letters*

*Roundtables*

**28 May 2014**

**Final Standard (IFRS)**

IFRS 15 *Revenue from Contracts with Customers*

Effective date: 1 Jan 2017

# Transition, effective date and early application



| | | PY2 (2015) | PY1 (2016) | | CY (2017) | CY footnotes |
|---|---|---|---|---|---|---|
| **Retrospective** (with optional practical expedients) | Cumulative catch-up | Contracts under new standard<br>Contracts restated | | | | |
| | | | | | | |
| **Cumulative effect at date of application** | | Contracts **not** restated | | Cumulative catch-up | Existing* and new contracts under new standard | Existing and new contracts presented under legacy IFRS/US GAAP |

*contracts not completed in prior years as determined under legacy revenue guidance

- Effective date: annual reporting periods beginning on or after 1 January 2017
- Early application permitted (IFRS only)



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# Overview of revenue proposals



## Core principle:

Recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services

## Steps to apply the core principle:

1. Identify the contract(s) with the customer
2. Identify the separate performance obligations
3. Determine the transaction price
4. Allocate the transaction price
5. Recognize revenue when a performance obligation is satisfied

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# Scope

- ✓ All contracts with customers, except
  - ✘ Lease contracts
  - ✘ Insurance contracts
  - ✘ Financial instruments
  - ✘ Non-monetary exchanges in the same line of business to facilitate sales to customers

# Step 1: Identify the contract



## Existence of a contract

- Must meet specified criteria to apply the model

## Combine contracts

- Negotiated as a package
- Linked consideration
- Goods or services form one performance obligation

## Contract modifications

- Separate contract if add distinct goods/services at standalone selling price
- Prospective if remaining goods/services distinct
- Otherwise, cumulative catch-up

# Step 2: Identify the performance obligations



## Promise to transfer a distinct good or service

**Customer can benefit from good or service**

- On its own
- Together with other readily available goods or services (including goods or services previously acquired from entity)

**Promised good or service is separable from other promises**

- No significant service of integrating the good or service
- Good or service does not significantly modify or customise another good or service in the contract
- Good or service is not highly dependent on or interrelated with other goods or services

# Step 3: Determine the transaction price



**Amount of consideration to which entity expects to be entitled in exchange for goods or services**

### Variable consideration

Estimate using:
- Expected value
- Most likely amount

but 'Constrained'

### Significant financing

Adjust consideration if timing provides customer or entity with significant benefit of financing

### Non-cash consideration

Measure at fair value unless cannot be reasonably estimated

### Consideration payable to customer

Reduction of the TP unless in exchange for a distinct good or service



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# Step 3: Constraining variable consideration



**Include estimate of variable consideration in the transaction price to extent it is highly probable a significant reversal of revenue will not occur as a result of a change in that estimate**

- Entity’s expectations of revenue reversal assessed using indicators, eg
  - Factors outside entity’s influence (market, 3rd-party actions)
  - Entity’s level of experience with similar types of contracts
  - Length of time before uncertainty resolved

# Step 4: Allocate the transaction price



Allocate to each performance obligation the amount to which entity expects to be entitled in exchange for satisfying that performance obligation

- Relative stand-alone selling price basis
  - estimate selling prices if not observable
  - residual estimation techniques may be appropriate
- Discounts and contingent amounts allocated entirely to specific performance obligation if specified criteria met

# Step 5: Recognise revenue when (as) a performance obligation is satisfied



Performance obligation is satisfied by transferring good or service

| Performance obligations satisfied over time if specified criteria met | All other performance obligations satisfied at a point in time |
|---|---|
| Revenue is recognised by measuring progress towards complete satisfaction of the performance obligation<br>• Clarified units produced or delivered may be a reasonable proxy in some cases<br>• Clarified input methods may need to be adjusted (eg uninstalled materials) | Revenue is recognised at the point in time when the customer obtains control of the promised asset. Indicators of control include:<br>• Present right to payment<br>• Legal title<br>• Physical possession<br>• Risks and rewards of ownership<br>• Customer acceptance |

# Step 5: Performance obligations satisfied over time



A performance obligation is satisfied over time (ie revenue recognised over time) if one of three criteria are met:

- The customer receives and consumes the benefits of the entity's performance as the entity performs
  - assessed by considering (hypothetically) whether another entity would need to substantially re-perform the work completed to date if that other entity were to fulfil the remaining obligation
- The entity's performance creates or enhances an asset (eg WIP) that the customer controls as the asset is created or enhanced
- The entity's performance does not create an asset with an alternative use to the entity and the entity has a right to payment for performance completed to date, and it expects to fulfil the contract as promised

# Contract costs



| Costs of obtaining a contract | Costs of fulfilling a contract | Onerous contracts |
| --- | --- | --- |
| Recognised as an asset if:<br>• Incremental<br>• Expected to be recovered<br><br>*For example:*<br>*Selling commissions* | Recognised as an asset if:<br>• Relate directly to a contract<br>• Relate to future performance<br>• Expected to be recovered<br><br>*For example: Pre-contract or setup costs* | Apply IAS 37 |

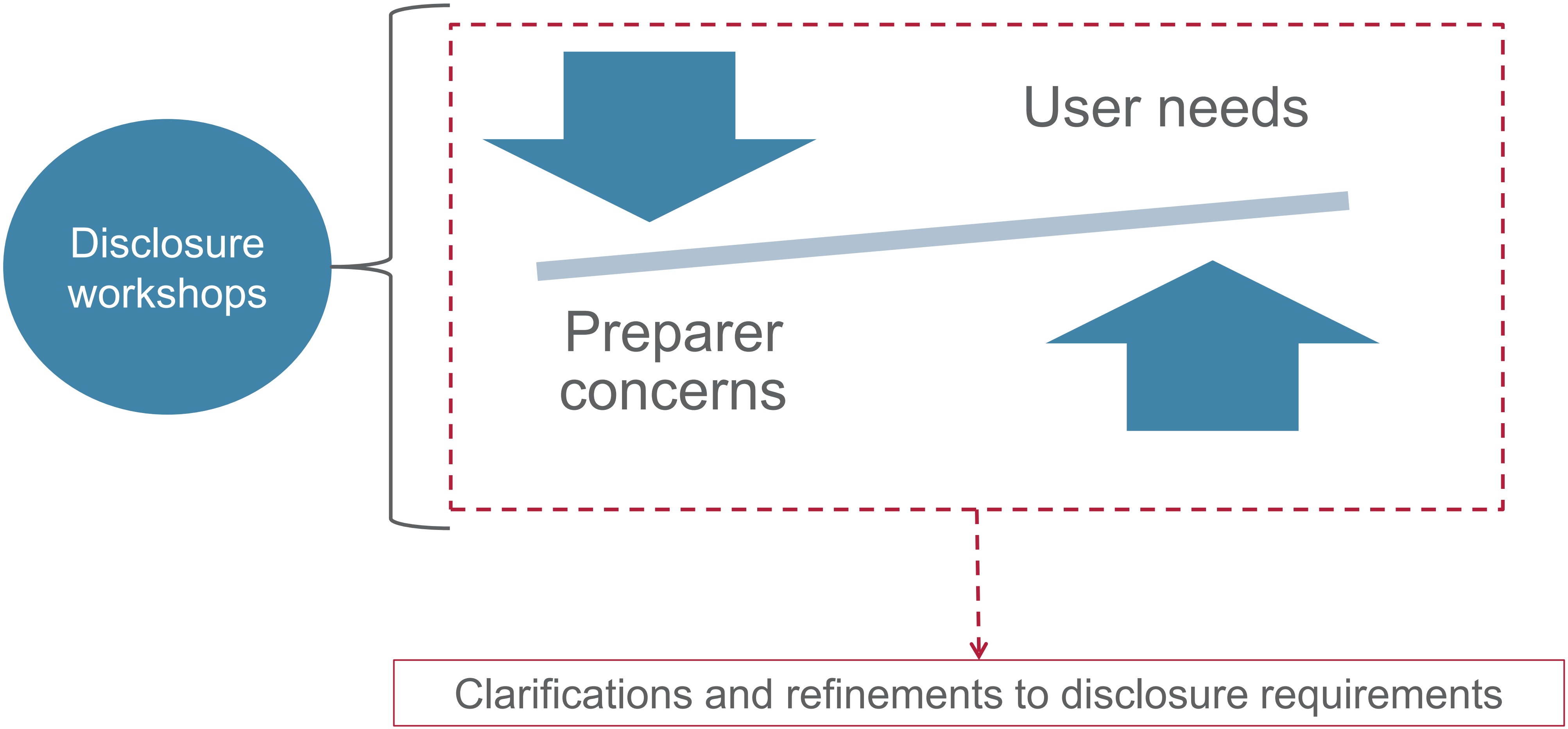
# Application guidance



- rights of return
- warranties
- principal or agent
- customer options
- non-refundable upfront fees
- licensing
- repurchase agreements
- consignment arrangements
- bill & hold
- customer acceptance

# Disclosure requirements





# Disclosure requirements (continued)



*Disclosure objective:* To enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers

**Disaggregation of revenue**

*Disaggregate revenue into categories that depict how revenue and cash flows are affected by economic factors*

- When determining categories, consider: other disclosures, information reviewed by chief operating decision maker and other information used by entity
- Explain relationship with segment disclosures

# Disclosure requirements (continued)



**Information about contract balances**

*A combination of qualitative and quantitative disclosures*

- Opening and closing balances
- Amount of revenue recognised from contract liabilities
- Explanation of significant changes in contract balances

**Remaining performance obligations**

- Disclose aggregate amount of the transaction price allocated to remaining performance obligations
- Quantitative or qualitative explanation of when amounts will be recognised as revenue

**Interim requirements**

*IASB* Disaggregation of revenue required in annual and interim financial statements; otherwise general principles of interim financial reporting apply

*FASB* All quantitative disclosures in annual and interim

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# Revenue Transition Resource Group



- Public discussion to support initial application of the new Revenue Standard
- Will **not** issue authoritative guidance
- Limited life group