REVENUE

Introduction

The International Accounting Standards Board (IASB) has issued a new standard, IFRS 15 *Revenue from Contracts with Customers* on 28 May 2014 which replaces IAS 18 *Revenue*, IAS 11 *Construction contracts* and related Interpretations*.* The standard is a result of a convergence process between the IASB and the Financial Accounting Standards Board (FASB). The revenue standard will be introduced into the FASB's Accounting Standards Codification as Topic 606, Update 2014-09, *Revenue from Contracts with Customers* which replaces the previous revenue guidance included in Topic 605.

Scope

The new revenue model would apply to all contracts with customers except leases, insurance contracts, financial instruments, guarantees and certain non-monetary exchanges. The sale of non-monetary financial assets, such as property, plant and equipment, real estate or intangible assets will also be required to follow some of the requirements of the new model.

Overview of the new revenue recognition model

The core principle of the new revenue model is that an entity should recognize revenue to depict the transfer of promised goods or services to the customer in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

The model is to be applied on an individual contract basis. However, as a practical expedient,a portfolio approach is permitted for contracts with similar characteristics provided it is reasonably expected that the impact on the financial statements will not be materially different from applying this model to the individual contracts.

To recognise revenue the following five steps should be applied:

The standard applies the same five step model to revenue recognition as the 2010 Exposure Draft (ED), however there have been many changes to the detailed requirements and the guidance. It is therefore advisable that entities do not rely on previous analysis as these may no longer be appropriate, but rather consider the details of the new standard cautiously.

Main differences between the IASB and the FASB revenue standards

Although the new revenue recognition standard is nearly fully converged, there are three main differences that exist which are explained below.

Timing of adoption

For entities using IFRS, the standard is effective for periods beginning on or after 1 January 2017 with early application permitted. For public entities using US GAAP, the standard is applicable for periods beginning after 15 December 2016, including the interim reporting periods therein. US private entities are required to apply the standard for annual reporting periods beginning after 15 December 2017, and interim and reporting periods thereafter.

Interim disclosures

IAS 34 *Interim Financial Reporting* was amended by the IASB to require an entity to disclose disaggregated revenue information in interim financial reports. The IASB further decided that for all other disclosures related to revenue from contracts with customers, the general principles of IAS 34 should apply. The FASB however decided that the same quantitative disclosures about revenue required for annual financial statements shall also be required in the interim financial reports excluding the disclosures related to costs.

The collectability threshold for contracts

The revenue model contains a collectability threshold that contracts must meet for revenue to be recognized. Entities would have to determine that collectability is probable in order to recognize revenue. This therefore introduces a slight divergence as “probable” has different meanings under IFRS and US GAAP. “Probable” means “more likely than not” under IFRS and “likely to occur” under US GAAP.

Effective date and transition

IFRS 15 is effective for annual periods beginning on or after 1 January 2017 with early application permitted. It applies to existing contracts that are not yet complete as of the effective date and new contracts entered into on or after the effective date. Therefore, in the first year of adoption, the current year figures will be measured and disclosed as if the new revenue model had always be applied.

Entities are allowed to choose whether to apply IFRS 15 retrospectively to each prior period presented (with optional practical expedients) or retrospectively according to an alternative transition method. Under the alternate transition method, restatement of comparative years is not required but the cumulative effect of initially applying IFRS 15 should be recognized as an adjustment to the opening retained earnings on the effective date.

Impact of the new standard

The issued standard does not vary significantly from the 2011 ED. Changes made were to further clarify and refine proposals made in the 2011 ED.

Almost all entities that generate revenue will be affected by the issue of this new standard. The new standard may result in substantial changes to the timing of revenue recognition. Sectors that will be most affected include construction, telecommunications and entertainment and media.

Although the effective date is years away, entities should begin the process of assessing the impact of the standard and the changes that will be required. For some entities, the transition may mean new calculations, judgments and estimates, changes to processes, IT systems and internal controls. Entities should not leave it till too late to find out how the new standard will affect their business.