



VIRTUAL COACHING CLASSES ORGANISED BY BOS, ICAI

FINAL LEVEL PAPER 1: FINANCIAL REPORTING

IND AS 115 – REVENUE FROM CONTRACTS WITH CUSTOMERS

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Scope and exceptions

Scope and scope exceptions

What is in scope or affected by the standard?

- ▶ Contracts with customers
- ▶ Sale of some non-financial assets that are not an output of the entity's ordinary activities (e.g., property, plant and equipment, intangible assets)
- ▶ Capitalization of certain costs

What is not in scope?

- ▶ Leasing contracts
- ▶ Insurance contracts
- ▶ Financial instruments and other contractual rights and obligations
- ▶ Non-monetary exchanges between entities in the same line of business

Key Definitions

▶ **Contracts**

An agreement between two or more parties that creates enforceable rights and obligations.

▶ **Contract Asset**

An entity's right to consideration in exchange for goods or services that the entity has transferred to a customer when that right is conditioned on something other than the passage of time (for example, the entity's future performance).

▶ **Contract Liability**

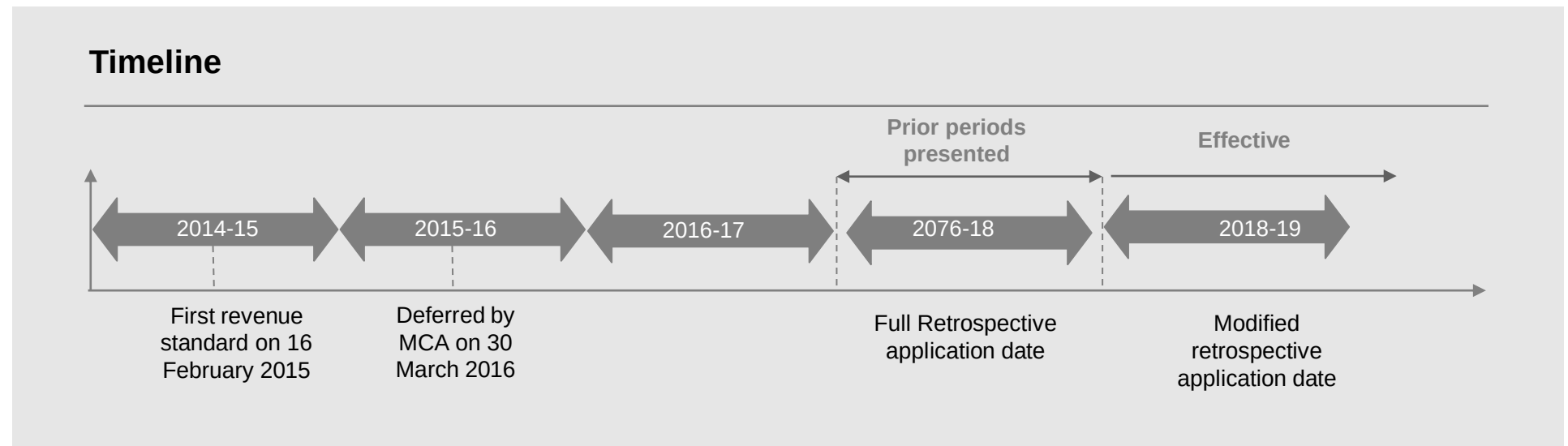
An entity's obligation to transfer goods or services to a customer for which the entity has received consideration (or the amount is due) from the customer.

▶ **Customer**

A party that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration.

Overview

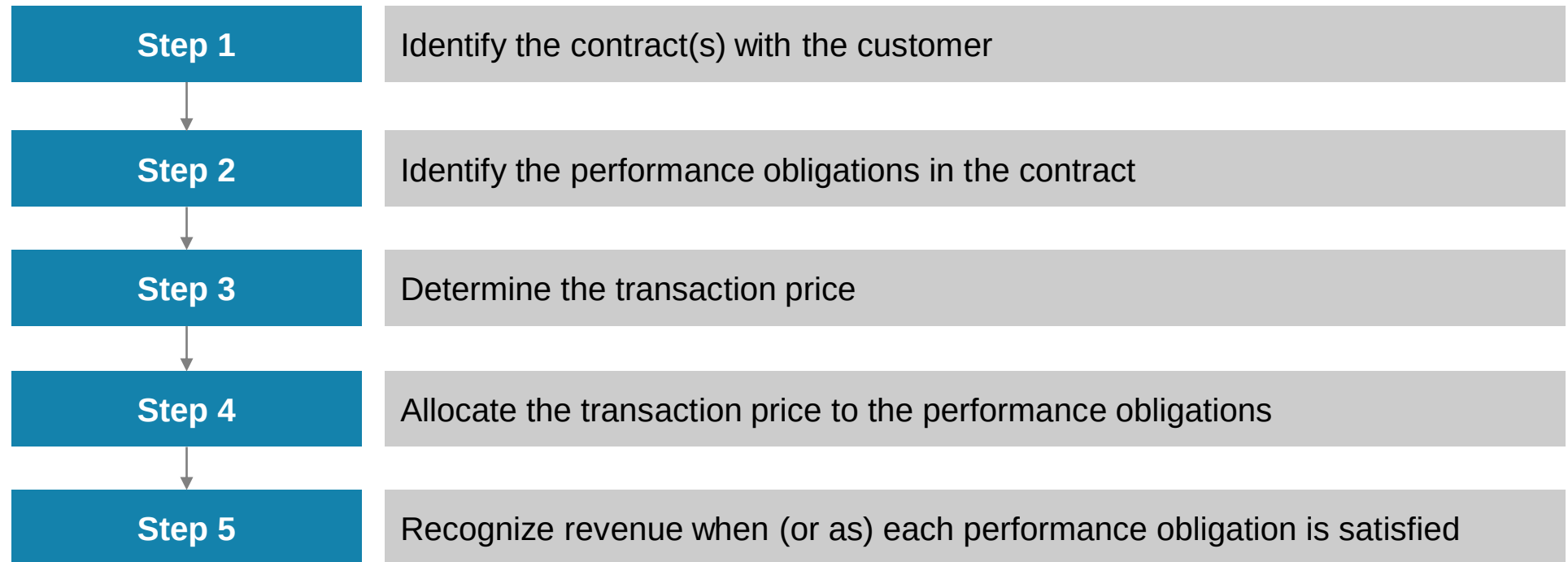
- ▶ Ind AS 115 Revenue from Contracts with Customers was first notified by MCA on 16 February 2015 and the applicability was deferred on 30 March 2016.
- ▶ The Exposure Draft released by ICAI on 26 April 2017 mentions that Ind AS 115 would be applicable for accounting periods beginning on or after 1 April 2018.
- ▶ It replaces all existing Ind AS revenue recognition requirements (Ind AS 11 and 18).
- ▶ Ind AS and IFRS revenue standards are substantially aligned, with some limited differences.
- ▶ The new framework focuses on the performance obligations in the contract and allocating a transaction price to those obligations.
- ▶ The new model is a control model, rather than a risk and reward model.



The five-step model

Summary of the model

Core principle: Recognize revenue to depict the transfer of promised 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



Transition methods

Transition

Ind AS 115 is effective for annual reporting periods beginning on or after 1 April 2018. Entities are required to apply the new revenue standard using either of the following two approaches:

- (a) Full retrospective approach: retrospectively to each prior period presented in accordance with Ind AS 8, subject to some practical expedients mentioned in the standard or
- (b) Modified retrospective approach: retrospectively with the cumulative effect of initial application recognised at the date of initial application

When applying the full retrospective method, an entity shall restate all prior periods presented in accordance with Ind AS 8. This results in comparative statements in which all periods are presented as if Ind AS 115 had been in effect since the beginning of the earliest period presented.

When applying modified retrospective approach, an entity does not restate prior periods presented and the cumulative effect of initial application is recognised in the opening retained earnings of the first year of application of Ind AS 115.

Transition methods

- ▶ Retrospective adoption required
- ▶ Two approaches permitted:
 - ▶ Full retrospective adoption, with optional reliefs available
 - ▶ Modified retrospective application, with optional reliefs available
- ▶ Factors to consider include:
 - ▶ The number of contracts to be restated
 - ▶ The length of contracts: long-term vs short-term
 - ▶ The ability to obtain historical information

Full vs. modified retrospective adoption

	PY (2017-18)	CY (2018-19)	Disclosures
Full retrospective (with optional practical expedients)	Cumulative catch-up	Contracts under new standard Contracts restated	Ind AS 115 and Ind AS 8 disclosures apply
Modified retrospective (Cumulative effect at date of application)	Contracts <u>not</u> restated	Cumulative catch-up Existing* and new contracts under new standard	Existing and new contracts compared using current Ind AS (e.g., Ind AS 18) in CY

*Entities may elect either to apply Ind AS 115 only to contracts that are not completed, or to all contracts, including completed contracts, at the date of initial application.

Full retrospective adoption: optional reliefs

An entity can choose to apply one or more of the following reliefs:

- ▶ For completed contracts – an entity need not restate those that:

- ▶ Begin and end within the same annual reporting period

Or

- ▶ Are completed contracts at the beginning of the earliest period presented

- ▶ For completed contracts that have variable consideration – an entity may use the transaction price at the date the contract was completed rather than estimating variable consideration for comparative periods

Full retrospective adoption: optional reliefs (cont.)

An entity can choose to apply one or more of the following reliefs (cont.):

- ▶ For contracts that were modified before the beginning of the earliest period presented – an entity need not retrospectively restate the contract. Instead, it reflects the aggregate effect of all modifications before the beginning of the earliest period presented when:
 1. Identifying the satisfied and unsatisfied performance obligations
 2. Determining the transaction price
 3. Allocating the transaction price
- ▶ For reporting periods presented before the date of initial application – an entity need not disclose:
 - ▶ The transaction price allocated to the remaining performance obligations
 - ▶ An explanation of when the entity expects to recognise that amount as revenue

Modified retrospective adoption: optional relief

- ▶ For contracts that were modified before the selected date below – an entity need not retrospectively restate the contract. Instead, it reflects the aggregate effect of all modifications before the beginning of the earliest period presented when:
 - ▶ Identifying the satisfied and unsatisfied performance obligations
 - ▶ Determining the transaction price
 - ▶ Allocating the transaction price

An entity can choose to apply this practical expedient either to:

- ▶ All contract modifications that occur before the beginning of the earliest period presented
- Or
- ▶ All contract modifications that occur before the date of initial application

Step 1: Identify the contract(s) with the customer

Step 1

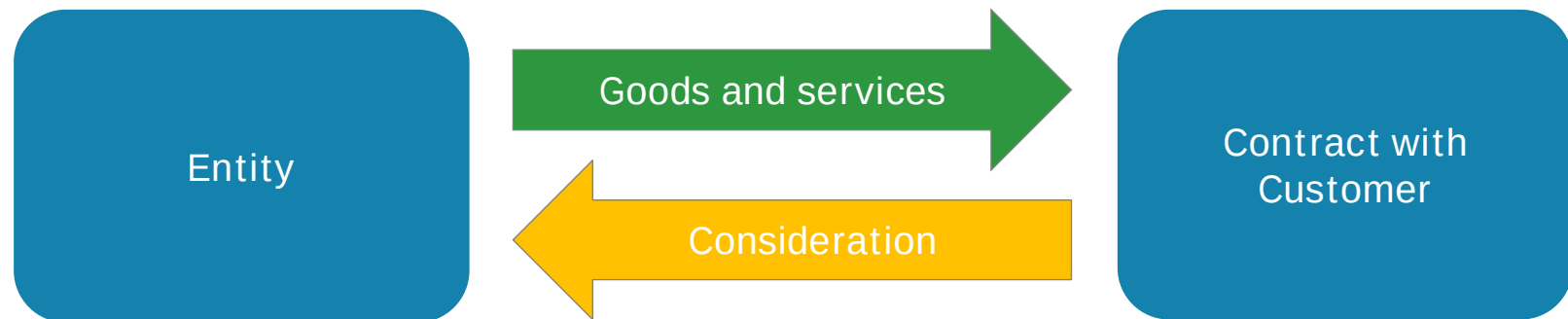
Identify the contract(s) with the customer

CONTRACT

- An agreement between two or more parties that creates enforceable rights and obligations.
- Contracts can be written, verbal or implied based on an entity's customary business practices.
- Does not exist if both parties can cancel without penalty.

CUSTOMER

- A party that has contracted with an entity to obtain goods or services in exchange for consideration.



Step 1

Identify the contract(s) with the customer

Contract term

- ▶ Entities should consider termination clauses when assessing contract term.
- ▶ If a contract can be terminated at any time for no compensation, the parties do not have enforceable rights and obligations, regardless of the stated term.
- ▶ In contrast, a contract that can be terminated early, but requires payment of a substantive termination penalty, is likely to have a contract term equal to the stated term. This is because enforceable rights and obligations exist throughout the stated contract period.
- ▶ Management should apply judgment in determining whether a termination penalty is substantive.

The contract term to which Ind AS 115 is applied may affect the number of performance obligations identified and the determination of the transaction price. It may also affect the amounts disclosed in some of the required disclosures.

Step 1

Identify the contract(s) with the customer

Example

- ▶ Service Provider enters into a contract with a customer to provide monthly services for a three-year period. Each party can terminate the contract at the end of any month for any reason without compensating the other party (that is, there is no penalty for terminating the contract early).
- ▶ What is the contract term for purposes of applying the revenue standard?

Solution

- ▶ The contract should be treated as a month-to-month contract despite the three-year stated term. The parties do not have enforceable rights and obligations beyond the month (or months) of services already provided.

Step 1

Identify the contract(s) with the customer

Example

A gymnasium enters into a contract with a new member to provide access to its gym for a 12-month period at Rs. 4,500 per month. The member can cancel his or her membership without penalty after three months. Specify the contract term.

Solution

The enforceable rights and obligations of this contract are for three months, and therefore the contract term is three months.

Step 1

Identify the contract(s) with the customer

Collectability criterion

- ▶ Collectability refers to the customer's intent and ability to pay the amount of promised consideration.
- ▶ If the threshold is not met, the contract should not be accounted for under the model until collectability concern is resolved.
- ▶ Collectability assessment relates to the transaction price.
- ▶ The transaction price may be less than the stated contract price if the entity intends to offer a price concession.
- ▶ Significant judgment will be required to determine if a partial payment is an implied price concession or an impairment loss.
- ▶ Entities should evaluate and update internal controls.

Step 1

Identify the contract(s) with the customer

Example

- ▶ An entity sells 1,000 units of a prescription drug to a customer for promised consideration of CU1 million
- ▶ This is the entity's first sale to a customer in a new region experiencing significant economic difficulty, and the entity expects that it will not be able to collect the full amount of promised consideration
- ▶ The entity determines that it expects to provide a price concession and accept a lower amount of consideration from the customer; the entity expects to be entitled to CU400,000
- ▶ The entity considers the customer's ability and intention to pay the estimated consideration and concludes that even though the region is experiencing economic difficulty, it is probable that it will collect CU400,000 from the customer

Step 1

Identify the contract(s) with the customer

Example

New way limited decides to enter a new market that is currently experiencing economic difficulty and expects that in future economy will improve. New way enters into an arrangement with a customer in the new region for networking products for promised consideration of Rs. 1,250,000. At contract inception, New way expects that it may not be able to collect the full amount from the customer.

Determine how New way will recognise this transaction?

Solution

Assuming the contract meets the other criteria covered within the scope of the model in Ind AS 115, New way need to assesses whether collectability is probable. In making this assessment, New way considers whether the customer has the ability and intent to pay the estimated transaction price, which may be an amount less than the contract price.

Step 1

Identify the contract(s) with the customer

Concept of commercial substance

Requirement under Ind AS 115

A contract to have commercial substance (i.e., the risk, timing or amount of the entity's future cash flows is expected to change as a result of the contract)

Need for such requirement

To prevent entities from artificially inflating revenue

Onus to substantiate commercial substance

In a change from legacy guidance, the entity should be able to demonstrate a substantive business purpose exists, considering the nature and structure of its transactions.

Step 1

Identify the contract(s) with the customer

Combining contracts

Are the contracts entered into at or near the same time with the same customer or related parties of the customer?

NO



Account for as
separate
contracts



YES

Are one or more of the following criteria met?

- ▶ Contracts are negotiated as a single commercial package
- ▶ Consideration in one contract depends on the other contract
- ▶ Goods or services are single performance obligation

NO



Account for as
separate
contracts



YES

Account for contracts together as a single contract

Contracts may be combined in a portfolio with similar characteristics if the entity reasonably expects the effects on the financial statements would not materially differ

Step 1

Identify the contract(s) with the customer

Example

Manufacturer of airplanes for the air force negotiates a contract to design and manufacture new fighter planes for a Kashmir air base. At the same meeting, the manufacturer enters into a separate contract to supply parts for existing planes at other bases. Would these contracts be combined?

Solution

Contracts were negotiated at the same time, but they appear to have separate commercial objectives. Manufacturing and supply contracts are not dependent on one another, and the planes and the parts are not a single performance obligation. Therefore, contracts for supply of fighter planes and supply of parts shall not be combined and instead, they shall be accounted separately.

Step 1

Identify the contract(s) with the customer

Contract Modification

A contract modification is a change in the scope and/or price of a contract, approved by the parties.

Accounting treatment depends on nature of modification

Separate contract

- Scope of the contract changes due to added goods or services that are distinct

And

- Price of the contract increases by the stand-alone selling price of the added goods or services

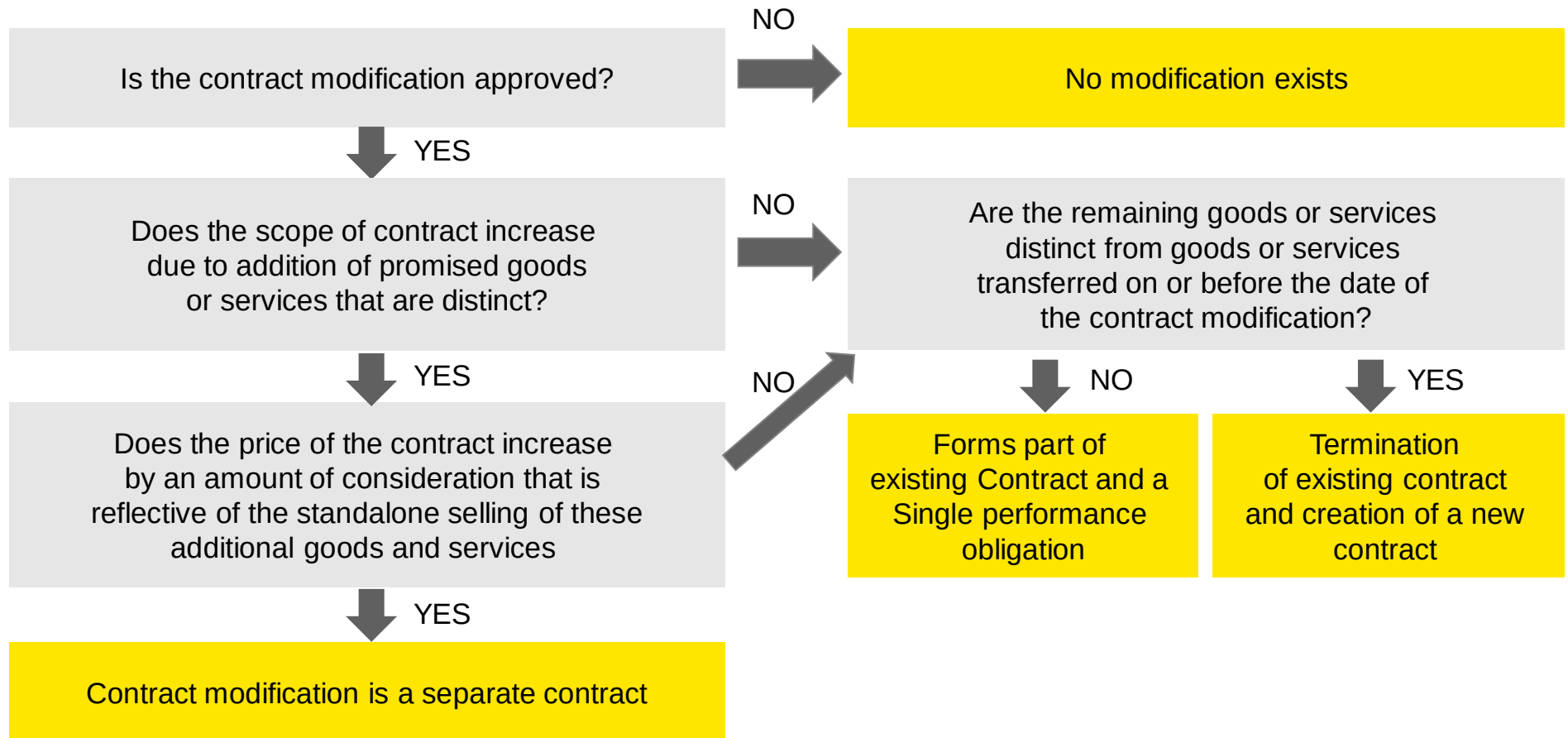
Part of original contract

- All other modifications

Step 1

Identify the contract(s) with the customer

Contract Modification



Step 1

Identify the contract(s) with the customer

Contract Modification

Modifications considered part of the original contract are accounted for differently, depending on the attributes of the remaining goods and/or services

Modification type	Accounting result
Goods and services not yet provided are distinct from the goods and services transferred on or before the modification	Allocate the remaining transaction price (consideration from original contract that was not recognized as revenue, and consideration from modification) to the remaining performance obligations – new contract
All promised goods and services (including those not yet provided or only partially provided) are part of a single performance obligation that is not fully satisfied at modification date	Update the transaction price and measure of progress toward completion; record an adjustment to revenue for the effect of the modification (i.e., a cumulative catch-up adjustment)
Goods and services not yet provided are a combination of two scenarios above	Completed performance obligations (and the related revenue) are not adjusted; open performance obligations are adjusted (as discussed above)

Step 1

Identify the contract(s) with the customer

Example

On 1 April, 20X1, KLC Ltd. enters into a contract with Mr. K to provide

- A machine for Rs. 2.5 million
- One year of maintenance services for Rs.55,000 per month

On 1 October 20X1, KLC Ltd. and Mr. K agree to modify the contract to reduce the amount of services from Rs. 55,000 per month to Rs. 45,000 per month.

Determine the effect of change in the contract?

Step 1

Identify the contract(s) with the customer

Solution

The next six months of services are distinct from the services provided in the first six months before modification in contract,

Therefore, KLC Ltd. will account for the contract modification as if it were a termination of the existing contract and the creation of a new contract.

The consideration allocated to remaining performance obligation is Rs. 270,000, which is the sum of

- The consideration promised by the customer (including amounts already received from the customer) that was included in the estimate of the transaction price and had not yet been recognized as revenue. This amount is zero.
- The consideration promised as part of the contract modification ie Rs. 270,000.

Step 1

Identify the contract(s) with the customer

Example

Growth Ltd enters into an arrangement with a customer for infrastructure outsourcing deal. Based on its experience, Growth Ltd determines that customising the infrastructure will take approximately 200 hours in total to complete the project and charges Rs. 150 per hour. After incurring 100 hours of time, Growth Ltd and the customer agree to change an aspect of the project and increases the estimate of labour hours by 50 hours at the rate of Rs. 100 per hour.

Determine how contract modification will be accounted as per Ind AS 115?

Step 1

Identify the contract(s) with the customer

Solution

Considering that the remaining goods or services are not distinct, the modification will be accounted for on a cumulative catch up basis, as given below:

Particulars	Hours	Rate(Rs.)	Amount(Rs.)
Initial contract amount	200	150	30000
Modification in contract	50	100	<u>5000</u>
Contract amount after modification	250	140*	<u>35000</u>
Revenue to be recognised	100	140	14000
Revenue already booked	100	150	15000
Adjustment in revenue			(1000)

$$*35,000 / 250 = 140$$

Step 1

Identify the contract(s) with the customer

Example

An entity promises to sell 120 products to a customer for Rs. 120,000 (Rs. 1,000 per product). The products are transferred to the customer over a six-month period. The entity transfers control of each product at a point in time. After the entity has transferred control of 60 products to the customer, the contract is modified to require the delivery of an additional 30 products (a total of 150 identical products) to the customer at a price of Rs. 950 per product which is the standalone selling price for such additional products at the time of placing this additional order . The additional 30 products were not included in the initial contract. It is assumed that additional products are contracted for a price that reflects the stand-alone selling price. Determine the accounting for the modified contract?

Solution

When the contract is modified, the price of the contract modification for the additional 30 products is an additional Rs. 28,500 or Rs. 950 per product. The pricing for the additional products reflects the stand-alone selling price of the products at the time of the contract modification and the additional products are distinct from the original products. Accordingly, the contract modification for the additional 30 products is, in effect, a new and separate contract for future products that does not affect the accounting for the existing contract and Rs. 950 per product for the 30 products in the new contract.

Step 1

Identify the contract(s) with the customer

Solution

When the contract is modified, the price of the contract modification for the additional 30 products is an additional Rs. 28,500 or Rs. 950 per product. The pricing for the additional products reflects the stand-alone selling price of the products at the time of the contract modification and the additional products are distinct from the original products. Accordingly, the contract modification for the additional 30 products is, in effect, a new and separate contract for future products that does not affect the accounting for the existing contract and Rs. 950 per product for the 30 products in the new contract.

Step 1

Identify the contract(s) with the customer

Example

Manufacturer enters into an arrangement with a customer to sell 100 goods for CU10,000 (CU100 per good). The goods are distinct and are transferred to the customer over a six-month period. The parties modify the contract in the fourth month to sell an additional 20 goods for CU95 each. The price of the additional goods represents the stand-alone selling price on the modification date.

Should Manufacturer account for the modification as a separate contract?

Solution

Yes. The modification to sell an additional 20 goods at CU95 each should be accounted for as a separate contract because the additional goods are distinct and the price reflects their stand-alone selling price. The existing contract would not be affected by the modification.

Step 1

Identify the contract(s) with the customer

Contract Modification – Example 2

► **Scenario A modification:**

- Vendor agrees to increase the number of cartridges to be delivered by 50 units
- Contract modification price per unit is CU1,250
- Current stand-alone selling price is CU1,250
- Additional units would be considered a separate contract

► **Scenario B modification:**

- Vendor agrees to increase the number of cartridges to be delivered by 50 units
- Contract modification price per unit is CU1,000, which is less than the current stand-alone selling price of CU1,250
- Vendor would have to determine whether the CU1,000 reflects the stand-alone selling price based on the specific facts and circumstances of the transaction
- Assuming that the remaining goods or services are not distinct from goods or services transferred on or before the date of the contract modification, the new contract should form part of the existing contract and, thus, a single performance obligation

Step 1

Identify the contract(s) with the customer

Is Purchase Order (PO) a contract ?

- ▶ The Purchase orders from Customers are contracts as it satisfy the below conditions –.
 - a. It creates enforceable right and obligation.
 - b. The PO specifies the goods required to be transferred and the rights with regards to the same are specified. The transaction price and payment terms are stated in the contract.
 - c. The contract has a commercial substance.
 - d. Customers have the ability and intent to pay the amount of consideration to which the company will be entitled to.

Step 2: Identify the performance obligations in the contract

Step 2:

Identify the performance obligations

Overview

Performance obligation

A performance obligation is a promise (explicit or implicit) to transfer to a customer either:

- ▶ A distinct good or service
- ▶ A series of distinct goods or services that are substantially the same and have the same pattern of transfer

Determining performance obligations

Performance obligations are identified at contract inception and determined based on:

- ▶ Contractual terms
- ▶ Customary business practices

Marketing incentives

Incidental obligations or marketing incentives may be performance obligations (e.g., “free” maintenance provided by automotive manufacturers, loyalty points provided by a hotel)



Does not include activities to satisfy an obligation (e.g., set-up activities) unless a good or service is transferred

Step 2:

Identify the performance obligations

Two-step model to identify which goods or services are distinct

Step 1:

Focus on whether the good or service is *capable of being distinct*

Customer can benefit from the individual good or service on its own

OR

Customer can use good or service with other readily available resources

Step 2:

Focus on whether the good or service is *distinct in the context of the contract*

- ▶ Evaluate whether multiple promised goods or services work together to deliver a combined output(s)
- ▶ Assess whether the good or service is integrated with, highly interdependent on, highly interrelated with, or significantly modifying or customising, other promised goods or services in the contract

Step 2:

Identify the performance obligations

Series of distinct goods and services



If a good or service is part of a series of distinct goods or services that are substantially the same and have the same pattern of transfer, the series must be treated as one performance obligation if:



Each distinct good or service in the series represents a performance obligation satisfied over time



The same method of progress is used to measure the transfer of each distinct good or service in the series to the customer

Step 2:

Identify the performance obligations

Performance obligations - Example 1

- ▶ Entity enters into a contract to manufacture and install customized equipment and provide maintenance services for a five-year period.
- ▶ Installation services include the integration of multiple pieces of equipment at the customer's facility in order for the equipment to operate as a single unit.
- ▶ Equipment cannot operate without installation
- ▶ Entity sells equipment and installation services together; does not sell installation separately
- ▶ Other vendors can provide the installation services
- ▶ The maintenance services are sold separately

Step 2:

Identify the performance obligations

Performance obligations - Solution 1

	Step 1 – Capable of being distinct	Step 2 – Distinct in the context of the contract
Equipment	Good cannot be used without installation, but customer can obtain installation from another source. Good is distinct. Move to Step 2.	Equipment and installation are highly interrelated. Significant customisation is required during installation. Good isn't distinct on its own because it must be combined with installation.
Installation	Installation can be provided by multiple vendors, so service is distinct. Move to Step 2.	See discussion above. Equipment and installation are not distinct from one another.
Maintenance	Services have a distinct function because they are sold separately. Move to Step 2.	Services are not highly interrelated. No integration, modification or customisation required. Services are individually distinct.

In this example, there are two performance obligations: (1) the equipment and the installation because they are distinct within the context of the contract; (2) maintenance services because they are distinct services.

Step 2:

Identify the performance obligations

Performance obligations - Example 2

- ▶ Contractor enters into a contract to design and build a house for a new homeowner.
- ▶ Contractor is responsible for the overall management of the project and identifies various goods and services that are provided, including architectural design, site preparation, construction of the home, plumbing and electrical services, and finish carpentry.
- ▶ Contractor regularly sells these goods and services individually to customers.

How many performance obligations are there in the contract?

Step 2:

Identify the performance obligations

Performance obligations - Solution 2

Step 1

- ▶ The promised goods and services are capable of being distinct because the homeowner could benefit from the goods or services either on their own or together with other readily available resources.
- ▶ This is because Contractor regularly sells the goods or services separately to other homeowners and the homeowner could generate economic benefit from the individual goods and services by using, consuming, or selling them.

Step 2

- ▶ However, the goods and services are not distinct within the context of the contract because they are not separately identifiable from other promises in the contract.
- ▶ Contractor provides a significant service of integrating the various goods and services into the home that the homeowner has contracted to purchase.

Thus, there is only one performance obligation.

Step 2:

Identify the performance obligations

Performance obligations - Example 3

- ▶ Software Co enters into a contract with a customer to provide a perpetual software license, installation services, and three years of post contract customer support (unspecified future upgrades and telephone support).
- ▶ The installation services require the entity to configure certain aspects of the software, but do not significantly modify the software.
- ▶ These services do not require specialized knowledge; and other sophisticated software technicians could perform similar services.
- ▶ The software does not require the upgrades and telephone support in order for it to remain functional.

How many performance obligations are there in the contract?

Step 2:

Identify the performance obligations

Performance obligations - Solution 3

- ▶ Performance obligations are- software license, installation services, unspecified future upgrades and telephone support.
- ▶ The customer can benefit from the software (delivered first) because it is functional without the installation services, unspecified future upgrades/ telephone support.
- ▶ The customer can benefit from the subsequent installation services, unspecified future upgrades and telephone support together with the software, which it has already obtained.
- ▶ Software Co concludes that each good and service is separately identifiable because the installation services, unspecified future upgrades, and telephone support do not significantly modify or customize the software. Additionally the software and services are not being integrated into the output that the customer has contracted to receive.

Step 2:

Identify the performance obligations

Performance obligations - Example 4

Manufacturer enters into a contract with a customer to sell a custom tool and replacement parts manufactured for the custom tool. Manufacturer only sells custom tools and replacement parts together, and no other entity sells either product. The customer can use the tool without the replacement parts, but the replacement parts have no use without the custom tool.

How many performance obligations are in the contract?

Step 2:

Identify the performance obligations

Performance obligations - Solution 4

- ▶ There are two performance obligations if Manufacturer transfers the custom tool first because the customer can benefit from the custom tool on its own and the customer can benefit from the replacement parts using a resource that is readily available to it (that is, the custom tool was transferred before the replacement parts).
- ▶ There is a single performance obligation if Manufacturer transfers the replacement parts first, because the customer cannot benefit from those parts without the custom tool, which is not a readily available resource in this fact pattern. The conclusion might differ if the custom tool was sold separately by Manufacturer or other entities.

Step 2:

Identify the performance obligations

Principal versus Agent Consideration

Determining whether an entity acts as a principal or an agent in a specific arrangement affects the amount of revenue recognized (gross versus net recognition)

Appropriately identifying the entity's performance obligation is fundamental to the principal or agent determination

Principal

- ▶ Provides goods or services itself

Agent

- ▶ Arranges for another party to provide goods or services

An entity is a principal if the entity controls a promised good or service before its transfer to a customer

An entity may not be a principal if it obtains legal title only momentarily before it is transferred to a customer

Step 2:

Identify the performance obligations

Principal versus Agent Consideration - Indicators

Indicators that an entity controls specified goods / services before it is transferred to customers –

Net Indicators:

Entity is primarily responsible for fulfilling the promise

Entity has the inventory risk

Entity has the discretion in establishing prices

Entity has the credit risk

Step 2:

Identify the performance obligations

Principal versus Agent Consideration – Recognizing Revenue

- ▶ Principal – Gross Amount
- ▶ Agent – Net Amount (the amount entity is entitled to retain)
- ▶ A principal would recognise revenue when (or as) it transfers the specified good or service to the customer.
- ▶ An agent would recognise revenue when its performance obligation to arrange for the specified good or service is complete

Step 2:

Identify the performance obligations

Principal vs Agent- Example

- ▶ TravelCo negotiates with major airlines to obtain access to airline tickets at reduced rates and sells the tickets to its customers through its website. TravelCo contracts with the airlines to buy a specific number of tickets at agreed-upon rates and must pay for those tickets regardless of whether it is able to resell them. Customers visiting TravelCo's website search TravelCo's available tickets. TravelCo has discretion in establishing the prices for the tickets it sells to its customers.
- ▶ TravelCo is responsible for delivering the ticket to the customer. TravelCo will also assist the customer in resolving complaints with the service provided by the airlines. The airline is responsible for fulfilling all other obligations associated with the ticket, including the air travel and related services (that is, the flight), and remedies for service dissatisfaction.

Is TravelCo the principal or agent for the sale of airline tickets to customers?

Step 2:

Identify the performance obligations

Principal vs Agent- Solution

Travel Co is the principal and should recognize revenue for the gross fee charged to customers. The specified good or service is a ticket that provides a customer with the right to fly on the selected flight (or another flight if the selected one is changed or cancelled). Travel Co controls the ticket prior to transfer of the ticket to the customer.

- ▶ Travel Co has the ability to direct the use of the ticket and obtains the remaining benefits from the ticket by reselling the ticket or using the ticket itself.
- ▶ Travel Co also has inventory risk before the ticket is transferred to the customer and discretion in establishing the price of the ticket.

The indicators therefore support that Travel Co is the principal.

Step 2:

Identify the performance obligations

Example

An entity negotiates with major airlines to purchase tickets at reduced rates compared with the price of tickets sold directly by the airlines to the public. The entity agrees to buy a specific number of tickets and will pay for those tickets even if it is not able to resell them. The reduced rate paid by the entity for each ticket purchased is negotiated and agreed in advance. The entity determines the prices at which the airline tickets will be sold to its customers. The entity sells the tickets and collects the consideration from customers when the tickets are purchased; therefore, there is no credit risk.

The entity also assists the customers in resolving complaints with the service provided by airlines. However, each airline is responsible for fulfilling obligations associated with the ticket, including remedies to a customer for dissatisfaction with the service. Determine whether the entity is a principal or an agent.

Step 2:

Identify the performance obligations

Solution

To determine whether the entity's performance obligation is to provide the specified goods or services itself (i.e. the entity is a principal) or to arrange for another party to provide those goods or services (i.e. the entity is an agent), the entity considers the nature of its promise. The entity determines that its promise is to provide the customer with a ticket, which provides the right to fly on the specified flight or another flight if the specified flight is changed or cancelled.

The entity considers the following indicators for assessment as principal or agent under the contract with the customers:

- (a) the entity is primarily responsible for fulfilling the contract, which is providing the right to fly. However, the entity is not responsible for providing the flight itself, which will be provided by the airline.
- (b) the entity has inventory risk for the tickets because they are purchased before they are sold to the entity's customers and the entity is exposed to any loss as a result of not being able to sell the tickets for more than the entity's cost.
- (c) the entity has discretion in setting the sales prices for tickets to its customers. The entity concludes that its promise is to provide a ticket (i.e. a right to fly) to the customer. On the basis of the indicators, the entity concludes that it controls the ticket before it is transferred to the customer. Thus, the entity concludes that it is a principal in the transaction and recognises revenue in the gross amount of consideration to which it is entitled in exchange for the tickets transferred.

Step 2:

Identify the performance obligations

- ▶ Rights of return
 - ▶ Does not represent a separate performance obligation
 - ▶ The impact should be considered when estimating the transaction price (as a component of variable consideration)
- ▶ Consignment arrangements
 - ▶ Standard includes indicators of a consignment arrangement
 - ▶ Revenue is not recognised when the goods are delivered to the consignee if control of the inventory has not been transferred



Step 2:

Identify the performance obligations

Example

Manufacturer M enters into a 60-day consignment contract to ship 1,000 dresses to Retailer A's stores. Retailer A is obligated to pay Manufacturer M Rs. 20 per dress when the dress is sold to an end customer.

During the consignment period, Manufacturer M has the contractual right to require Retailer A to either return the dresses or transfer them to another retailer. Manufacturer M is also required to accept the return of the inventory. State when the control is transferred.

Step 2:

Identify the performance obligations

Solution

Manufacturer M determines that control has not been transferred to Retailer A on delivery, for the following reasons:

- (a) Retailer A does not have an unconditional obligation to pay for the dresses until they have been sold to an end customer;
- (b) Manufacturer M is able to require that the dresses be transferred to another retailer at any time before Retailer A sells them to an end customer; and
- (c) Manufacturer M is able to require the return of the dresses or transfer them to another retailer.

Manufacturer M determines that control of the dresses transfers when they are sold to an end customer i.e. when Retailer A has an unconditional obligation to pay Manufacturer M and can no longer return or otherwise transfer the dresses.

Manufacturer M recognises revenue as the dresses are sold to the end customer.

Step 2:

Identify the performance obligations

Multiple Element Arrangements/ Goods and services that are not distinct

Once an entity determines whether the goods and services would be distinct based on their individual characteristics, the entity then has to consider if the manner in which the goods and services have been bundled in an arrangement would require the entity to account for two or more goods or services as one performance obligation. This determination would be required regardless of whether or not those goods and services were determined to be distinct on their own.

If the good or services are not considered as distinct, those goods or services are combined with other goods or services under the contract till the time the entity identifies a bundle of distinct goods or services.

This combination would result in accounting of multiple goods or services in the contract as a single performance obligation. This could also result in an entity combining a good or service that is not considered distinct with another good or service that, on its own, would have met the criteria to be considered distinct. An entity may end up accounting for all the goods or services promised in a contract as a single performance obligation if the entire bundle of promised goods and services is the only distinct performance obligation identified.

Step 2:

Identify the performance obligations

Example

Entity A, a specialty construction firm, enters into a contract with Entity B to design and construct a multi-level shopping centre with a customer car parking facility located in sub - levels underneath the shopping centre. Entity B solicited bids from multiple firms on both phases of the project — design and construction.

The design and construction of the shopping centre and parking facility involves multiple goods and services from architectural consultation and engineering through procurement and installation of all of the materials. Several of these goods and services could be considered separate performance obligations because Entity A frequently sells the services, such as architectural consulting and engineering services, as well as standalone construction services

based on third party design, separately. Entity A may require to continually alter the design of the shopping centre and parking facility during construction as well as continually assess the propriety of the materials initially selected for the project.

Determine how many performance obligations does the entity A have?

Step 2:

Identify the performance obligations

Solution

Entity A analyses that it will be required to continually alter the design of the shopping centre and parking facility during construction as well as continually assess the propriety of the materials initially selected for the project. Therefore, the design and construction phases are highly dependent on one another (i.e., the two phases are highly interrelated). Entity A also determines that significant customisation and modification of the design and construction services is required in order to fulfil the performance obligation under the contract. As such, Entity A concludes that the design and construction services will be bundled and accounted for as one performance obligation.

Step 2:

Identify the performance obligations

Example

An entity, a software developer, enters into a contract with a customer to transfer a software license, perform an installation service and provide unspecified software updates and technical support (online and telephone) for a two-year period. The entity sells the license, installation service and technical support separately. The installation service includes changing the web screen for each type of user (for example, marketing, inventory management and information technology). The installation service is routinely performed by other entities and does not significantly modify the software. The software remains functional without the updates and the technical support. Determine how many performance obligations does the entity have?

Step 2:

Identify the performance obligations

Solution

The entity assesses the goods and services promised to the customer to determine which goods and services are distinct. The entity observes that the software is delivered before the other goods and services and remains functional without the updates and the technical support. Thus, the entity concludes that the customer can benefit from each of the goods and services either on their own or together with the other goods and services that are readily available.

The entity also considers the factors of Ind AS 115 and determines that the promise to transfer each good and service to the customer is separately identifiable from each of the other promises. In particular, the entity observes that the installation service does not significantly modify or customise the software itself and, as such, the software and the installation service are separate outputs promised by the entity instead of inputs used to produce a combined output.

On the basis of this assessment, the entity identifies four performance obligations in the contract for the following goods or services:

- The software license
- An installation service
- Software updates
- Technical support

Step 2:

Identify the performance obligations

Example

The promised goods and services are the same as in the above Illustration, except that the contract specifies that, as part of the installation service, the software is to be substantially customised to add significant new functionality to enable the software to interface with other customised software applications used by the customer. The customised installation service can be provided by other entities.

Determine how many performance obligations does the entity have?

Step 2:

Identify the performance obligations

Example

The entity assesses the goods and services promised to the customer to determine which goods and services are distinct. The entity observes that the terms of the contract result in a promise to provide a significant service of integrating the licensed software into the existing software system by performing a customised installation service as specified in the contract. In other words, the entity is using the license and the customised installation service as inputs to produce the combined output (i.e. a functional and integrated software system) specified in the contract. In addition, the software is significantly modified and customised by the service. Although the customised installation service can be provided by other entities, the entity determines that within the context of the contract, the promise to transfer the license is not separately identifiable from the customised installation service and, therefore, the criterion on the basis of the factors is not met. Thus, the software license and the customised installation service are not distinct.

The entity concludes that the software updates and technical support are distinct from the other promises in the contract. This is because the customer can benefit from the updates and technical support either on their own or together with the other goods and services that are readily available and because the promise to transfer the software updates and the technical support to the customer are separately identifiable from each of the other promises.

Step 2:

Identify the performance obligations

Solution(cont.)

On the basis of this assessment, the entity identifies three performance obligations in the contract for the following goods or services:

- a) customised installation service (that includes the software license);
- b) software updates; and
- c) technical support.

Step 2:

Identify the performance obligations

Long term arrangements

Entities frequently enter into arrangements to provide services on a long-term basis, such as maintenance services to be provided over a long period of time.

For example, should a three-year maintenance agreement be considered a single performance obligation representing the entire contractual period, or should it be broken into smaller periods(daily, monthly or yearly)? It may be appropriate to treat a three-year services contract as three separate one-year performance obligations, if the contract can be renewed or cancelled by either party at discrete points in time (that is, at the end of each service year). The entity would separately account for its rights and obligations for each period in which the contract cannot be cancelled by either party.

In long-term service agreements when the consideration is fixed, the accounting generally will not change regardless of whether a single performance obligation or multiple performance obligations are identified.

Step 2:

Identify the performance obligations

Example

A cable company provides television services for a fixed rate fee of Rs. 800 per month for a period of 3 years. Cable services is satisfied overtime because customer consumes and receives benefit from services as it is provided i.e. customer generally benefits each day that they have access to cable service.

Determine how many performance obligations does the cable company have?

Step 2:

Identify the performance obligations

Solution

Cable company determines that each increment of its services e.g. day or month, is a distinct performance obligation because customer benefits from that period of services on its own. additionally, each increment of service is separately identifiable from those preceding and following it i.e. one service period does not significantly affect, modify or customise another. Therefore, it can be concluded that its contract with customer is a single performance obligation to provide three years of cable service because each of the distinct increments of service is satisfied over time. Also, cable company uses the same measure of progress to recognise revenue on its cable television service regardless of the contract's time period.

Step 2:

Identify the performance obligations

Non-refundable upfront fees

In some contracts, an entity charges the customer a non-refundable upfront fee. Examples include joining fees in health club membership, activation fees for telecom services, setup fees in certain service contracts and initial fees or joining fees in some supply contracts with the distributors or customers.

To identify performance obligations in such contracts, an entity shall assess whether the fee relates to an activity that the entity is required to undertake at the inception of the contract, or that activity does not result in the transfer of a promised good or service to the customer.

In many cases, even though a non-refundable upfront fee relates to an activity that the entity is required to undertake at or near contract inception to fulfil the contract, that activity does not result in the transfer of a promised good or service to the customer. Instead the upfront fee is an advance payment for future goods and services and, therefore, would be recognised as revenue when those future goods and services are provided.

If the non-refundable upfront fee relates to a goods or service, the entity shall evaluate whether to account for the goods or services as a separate performance obligation. An entity may charge a non-refundable as a part of compensation of costs incurred in setting up a contract (or other administrative tasks). If those setup activities do not satisfy performance obligation, the entity shall disregard those activities (and related costs) when measuring progress. That is because the costs of setup activities do not depict transfer of services to customer.

Step 2:

Identify the performance obligations

Example

Customer buy a new data connection from the telecom entity. It pays one-time registration and activation fees at the time of purchase of new connection.

The customer will be charged based on the usage of the data services of the connection on monthly basis.

Are the performance obligations under the contract distinct?

Step 2:

Identify the performance obligations

Solution

By selling a new connection, the entity promises to supply data services to customer. Customer will not be able to benefit from just buying a data card and data services from third party. The activity of registering and activating connection is not a service to customer and therefore does not represent satisfaction of performance obligation. Entity's obligation is to provide data service and hence activation is not a separate performance obligation.

Step 2:

Identify the performance obligations

Example

A retailer has a stated policy that any products may be returned within 30 days. Based on past pattern, 10% of goods purchased are returned within the 30 day window.

On March 15, 20XX, the retailer enters into a new contract and sells 100 units costing INR. 20 per unit at a price of INR. 30 per unit.

The retailer is unable to assert that it is highly probable a significant revenue reversal will not occur for the variable component (i.e., the 10%).

How revenue need to be recorded?

Step 2:

Identify the performance obligations

Example

The variable consideration (i.e., 10% of the transaction price subject to return) cannot be recognized until April 15, 20XX, when the 30-day right of return lapses.

Following entries will be made:

March 15, 20XX (On Sale of Product)

Dr Asset (right to recover product)	INR. 200	
Dr Cost of Sales	INR. 1,800	
Cr Inventory		INR. 2, 000
Dr Cash	INR. 3,000	
Cr Refund Liability		INR. 300
Cr Revenue		INR. 2,700

Step 2:

Identify the performance obligations

Example

April 15, 20XX When the 30-day refund period lapses (assuming no returns).

Dr Refund Liability	INR. 300	
Cr Revenue		INR. 300
Dr Cost of Sales	INR. 200	
Cr Asset (right to recover product)		INR. 200

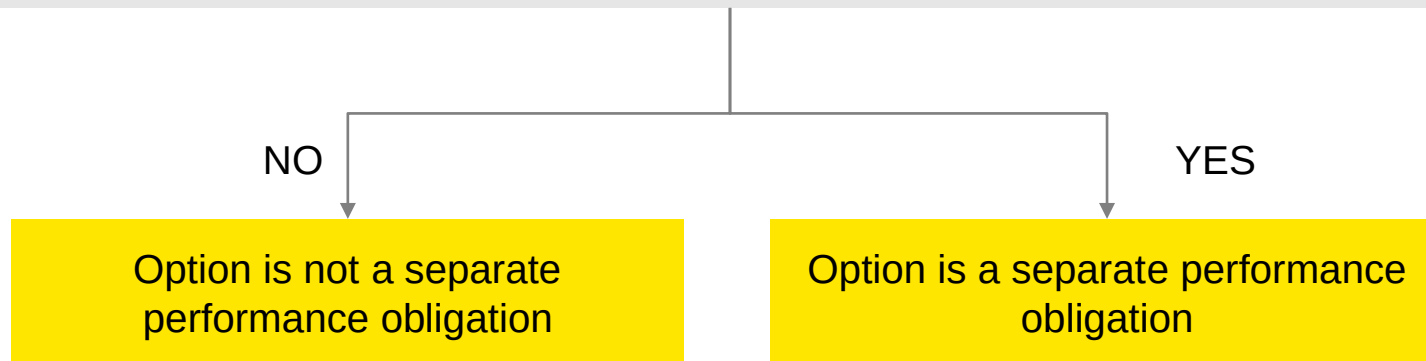
Step 2:

Identify the performance obligations

Options granting material rights

Does the contract grant the customer the option to acquire additional goods or services?

Does the option provide a material right to the customers that it would not receive without entering into the contract ?



Step 2:

Identify the performance obligations

Options granting material rights

Revenue is recognised when future goods and services are transferred or when the option expires

The transaction price is allocated to performance obligations (including the option) based on relative stand-alone selling prices

Estimate of stand-alone selling price of option reflects:

- ▶ The discount a customer receives when exercising the option, adjusted for the discount a customer receives without exercising the option and the likelihood the option will be exercised

As an alternative to estimating the stand-alone selling price of the option, an entity could evaluate the transaction assuming the option will be exercised

- ▶ Transaction price will be determined by including any consideration estimated to be received from the optional goods and services (variable consideration)
- ▶ Transaction price would be allocated to all goods and services (including those under option)
- ▶ Typically applied when original and additional goods are similar

Step 2:

Identify the performance obligations

Options granting material rights - Example

An entity enters into a contract with a customer A to sell garden supplies, and the arrangement includes a 40% discount voucher on future purchases

Simultaneous seasonal promotion gives all customers a 10% discount, therefore, customer A receives an incremental discount of 30% (40% discount in the contract less the 10% discount available to all customers)

Entity determines there is an 80% likelihood of redemption and estimates that customers will purchase (on average) CU50 of additional goods

Step 2:

Identify the performance obligations

Options granting material rights- Conclusion

- ▶ Entity estimates the stand-alone selling price of voucher as:
 - ▶ Average purchases x incremental discount x likelihood
 - ▶ $CU50 \times (40\% - 10\%) \times 80\% = CU12$

Step 2:

Identify the performance obligations

Warranties



Factors to consider when determining whether a warranty promise provides more than “quality assurance” include:

Is the warranty required by law?



A law requiring a warranty generally indicates the promised warranty is not a performance obligation

What is the length of the warranty coverage period?



The longer the warranty period, the more likely it is that the promised warranty is a separate performance obligation

What is the nature of the tasks that the entity promises to perform?



If it is necessary for an entity to perform specified tasks to provide the assurance that a product complies with agreed-upon specifications, then those tasks likely do not give rise to a performance obligation

Step 2:

Identify the performance obligations

Example

An entity enters into a contract for the sale of Product A for Rs.1,000. As part of the contract, the entity gives the customer a 40% discount voucher for any future purchases up to Rs. 1,000 in the next 30 days. The entity intends to offer a 10% discount on all sales during the next 30 days as part of a seasonal promotion. The 10% discount cannot be used in addition to the 40% discount voucher.

The entity believes there is 80% likelihood that a customer will redeem the voucher and on an average, a customer will purchase Rs. 500 of additional products.

Determine how many performance obligations does the entity have and their stand -alone selling price and allocated transaction price?

Step 2:

Identify the performance obligations

Solution

Since all customers will receive a 10% discount on purchases during the next 30 days, the only additional discount that provides the customer with a material right is the incremental discount of 30% on the products purchased. The entity accounts for the promise to provide the incremental discount as a separate performance obligation in the contract for the sale of Product A.

The entity believes there is 80% likelihood that a customer will redeem the voucher and on an average, a customer will purchase Rs. 500 of additional products. Consequently, the entity's estimated stand-alone selling price of the discount voucher is Rs. 120 (Rs. 500 average purchase price of additional products $\times$ 30% incremental discount $\times$ 80% likelihood of exercising the option). The stand-alone selling prices of Product A and the discount voucher and the resulting allocation of the Rs. 1,000 transaction price are as follows:

Performance Obligation	Stand-alone Selling Price
Product A	1000
Discount voucher	120
Total	1120

Step 2:

Identify the performance obligations

Solution(Cont.)

Performance obligations		Allocated transaction price (to nearest Rs.10)
Product A	$(Rs. 1000 \div Rs. 1120 \times Rs. 1000)$	890
Discount voucher	$(Rs. 120 \div Rs. 1120 \times Rs. 1000)$	110
Total		1000

The entity allocates Rs. 890 to Product A and recognises revenue for Product A when control transfers. The entity allocates Rs. 110 to the discount voucher and recognises revenue for the voucher when the customer redeems it for goods or services or when it expires.

Step 3: Determine the transaction price

Step 3:

Determine the transaction price Overview



Transaction price

Transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties

Transaction price reflects the effects of the following:



Variable consideration (including application of the constraint)



Significant financing component



Non-cash consideration



Consideration paid or payable to a customer

Step 3:

Determine the transaction price Variable consideration

- ▶ Transaction price may vary because of variable consideration
- ▶ Definition of “variable consideration” is broad
- ▶ Identifying variable consideration is an important step in the new model because the constraint has to be considered for each type of variable consideration

Common types and events that cause consideration to be variable

Bonuses

Incentive payments

Penalties

Refunds

Market-based fees

Discounts

Refunds

Money-back guarantees

Price concessions

Volume rebates

Service level agreements

Liquidating damages

Step 3:

Determine the transaction price Variable consideration

Estimating the transaction price

Variable consideration is estimated using the approach that better predicts the amount to which the company is entitled based on its facts and circumstances (i.e., not a “free choice”)



The approach should be applied consistently throughout the contract and for similar types of contracts

Expected value

- ▶ Sum of the probability-weighted amounts in a range of possible outcomes
- ▶ Most predictive when the transaction has a large number of possible outcomes
- ▶ Can be based on a limited number of discrete outcomes and probabilities

Most likely amount

- ▶ The single most likely amount in a range of possible outcomes
- ▶ May be appropriate when the transaction will produce only two outcomes

Step 3:

Determine the transaction price Variable consideration

Example

XYZ Limited enters into a contract with a customer to build a sophisticated machinery. The promise to transfer the asset is a performance obligation that is satisfied over time. The promised consideration is Rs.2.5 crores, but that amount will be reduced or increased depending on the timing of completion of the asset. Specifically, for each day after 31 March 20X1 that the asset is incomplete, the promised consideration is reduced by Rs. 1 lakh. For each day before 31 March 20X1 that the asset is complete, the promised consideration increases by Rs. 1 lakh.

In addition, upon completion of the asset, a third party will inspect the asset and assign a rating based on metrics that are defined in the contract. If the asset receives a specified rating, the entity will be entitled to an incentive bonus of Rs. 15 lakhs.
Determine the transaction price.

Step 3:

Determine the transaction price Variable consideration

Solution

In determining the transaction price, the entity prepares a separate estimate for each element of variable consideration to which the entity will be entitled using the estimation methods described in paragraph 53 of Ind AS 115:

- a) the entity decides to use the expected value method to estimate the variable consideration associated with the daily penalty or incentive (i.e. Rs. 2.5 crores, plus or minus Rs. 1 lakh per day). This is because it is the method that the entity expects to better predict the amount of consideration to which it will be entitled.
- b) the entity decides to use the most likely amount to estimate the variable consideration associated with the incentive bonus. This is because there are only two possible outcomes (Rs. 15 lakhs or Rs. Nil) and it is the method that the entity expects to better predict the amount of consideration to which it will be entitled.

Step 3:

Determine the transaction price Overview

Example

AST Limited enters into a contract with a customer to build a manufacturing facility. The entity determines that the contract contains one performance obligation satisfied over time. Construction is scheduled to be completed by the end of the 36th month for an agreed-upon price of Rs.25 crores.

The entity has the opportunity to earn a performance bonus for early completion as follows:

- 15 percent bonus of the contract price if completed by the 30th month (25% likelihood)
- 10 percent bonus if completed by the 32nd month (40% likelihood)
- 5 percent bonus if completed by the 34th month (15% likelihood)

In addition to the potential performance bonus for early completion, AST Limited is entitled to a quality bonus of Rs. 2 crores if a health and safety inspector assigns the facility a gold star rating as defined by the agency in the terms of the contract. AST Limited concludes that it is 60% likely that it will receive the quality bonus.

Determine the transaction price.

Step 3:

Determine the transaction price Overview

Solution(Cont.)

In determining the transaction price, AST Limited separately estimates variable consideration for each element of variability ie the early completion bonus and the quality bonus. AST Limited decides to use the expected value method to estimate the variable consideration associated with the early completion bonus because there is a range of possible outcomes and the entity has experience with a large number of similar contracts that provide a reasonable basis to predict future outcomes.

Step 3:

Determine the transaction price Overview

Solution

Therefore, the entity expects this method to best predict the amount of variable consideration associated with the early completion bonus. AST's best estimate of the early completion bonus is Rs. 2.13 crores, calculated as shown in the following table:

Bonus %	Amount of bonus (Rs. in crores)	Probability(%)	Probability-weighted amount (Rs. in crores)
15	3.75	25	.9375
10	2.50	40	1
5	1.25	15	.1875
0	-	20	-
			2.125

Step 3:

Determine the transaction price Overview

Solution(Cont.)

AST Limited decides to use the most likely amount to estimate the variable consideration associated with the potential quality bonus because there are only two possible outcomes (Rs. 2 crores or Rs. Nil) and this method would best predict the amount of consideration associated with the quality bonus. AST Limited believes the most likely amount of the quality bonus is Rs. 2 crores.

Step 3:

Determine the transaction price

Price concessions

Collecting less than the full price

Entering into a contract expecting to collect less than the full transaction price may indicate a price concession

Variable consideration

Price concessions (including implied price concessions) cause consideration to be variable and should not be included in the estimated transaction price

Transaction price

Existence of the contract

If an entity determines it is not probable of collecting the estimated transaction price, a valid contract does not exist (as discussed in Step 1 of the model)



When assessing Step 1 (identify the contract), an entity also must consider Step 3 of the model (determine the transaction price)



Distinguishing between customer credit risk (i.e., bad debt) and implied price concessions (i.e., reductions of revenue) will require significant judgement

Step 3:

Determine the transaction price

Constraint on Variable Consideration

- ▶ An entity should include an amount of variable consideration 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 resolved
- ▶ Objective of the constraint – include variable consideration in the transaction price only to the extent it is “Highly probable” that a significant revenue reversal will not occur when uncertainty is subsequently resolved
- ▶ “Significant” is relative to cumulative revenue recognized
- ▶ Indicators that suggest including the variable consideration in the transaction price could result in a significant revenue reversal include:
 - ▶ Consideration is highly susceptible to factors outside an entity’s influence (e.g., market volatility, weather conditions)
 - ▶ Uncertainty of variable amounts is not expected to be resolved for a long period of time
 - ▶ Entity’s experience with similar contracts is limited or has little predictive value
 - ▶ Entity has a practice of offering price concessions or changing payment terms and conditions
 - ▶ Contract has a large number and broad range of possible consideration amounts

Step 3:

Determine the transaction price Overview

Example

HT Limited enters into a contract with a customer on 1 April 20X1 to sell Product X for Rs. 1,000 per unit. If the customer purchases more than 100 units of Product A in a financial year, the contract specifies that the price per unit is retrospectively reduced to Rs. 900 per unit.

Consequently, the consideration in the contract is variable.

For the first quarter ended 30 June 20X1, the entity sells 10 units of Product A to the customer. The entity estimates that the customer's purchases will not exceed the 100 unit threshold required for the volume discount in the financial year. HT Limited determines that it has significant experience with this product and with the purchasing pattern of the customer. Thus, HT Limited concludes that it is highly probable that a significant reversal in the cumulative amount of revenue recognised (i.e. Rs. 1,000 per unit) will not occur when the uncertainty is resolved (i.e. when the total amount of purchases is known).

Step 3:

Determine the transaction price Overview

Example(Cont.)

Further, in May 20X1, the customer acquires another company and in the second quarter ended 30 September 20X1 the entity sells an additional 50 units of Product A to the customer. In the light of the new fact, the entity estimates that the customer's purchases will exceed the 100 unit threshold for the financial year and therefore it will be required to retrospectively reduce the price per unit to Rs. 900.

Determine the amount of revenue to be recognise by HT Ltd. for the quarter ended 30 June 20X1 and 30 September 20X1.

Step 3:

Determine the transaction price Overview

Solution

The entity recognises revenue of Rs. 10,000 ($10 \text{ units} \times \text{Rs. } 1,000 \text{ per unit}$) for the quarter ended 30 June 20X1. HT Limited recognises revenue of Rs. 44,000 for the quarter ended 30 September 20X1. That amount is calculated from Rs. 45,000 for the sale of 500 units ($50 \text{ units} \times \text{Rs. } 900 \text{ per unit}$) less the change in transaction price of Rs. 1,000 ($10 \text{ units} \times \text{Rs. } 100 \text{ price reduction}$) for the reduction of revenue relating to units sold for the quarter ended 30 June 20X1.

Step 3:

Determine the transaction price

Variable consideration – rights of return



- ▶ Rights of return are a form of variable consideration

Recognising revenue

Revenue recognition is limited to amounts for which it is 'highly probable' a significant reversal will not occur (i.e., it is highly probable the goods will not be returned)

Refund liability



A refund liability is established for the expected amount of refunds and credits to be issued to customers

Return assets



Corresponding asset and adjustment to cost of sales is recorded for items expected to be returned, based on carrying amount of the asset transferred less costs to recover

Return assets must be recorded separately from inventory



Return assets are subject to impairment review

Step 3:

Determine the transaction price Overview

Example

An entity enters into 1,000 contracts with customers. Each contract includes the sale of one product for Rs. 50 (1,000 total products × Rs. 50 = Rs. 50,000 total consideration). Cash is received

when control of a product transfers. The entity's customary business practice is to allow a customer to return any unused product within 30 days and receive a full refund. The entity's cost of each product is Rs. 30.

The entity applies the requirements in Ind AS 115 to the portfolio of 1,000 contracts because it reasonably expects that, in accordance with paragraph 4, the effects on the financial statements from applying these requirements to the portfolio would not differ materially from applying the requirements to the individual contracts within the portfolio. Since the contract allows a customer to return the products, the consideration received from the customer is variable.

To estimate the variable consideration to which the entity will be entitled, the entity decides to use the expected value method (see paragraph 53(a) of Ind AS 115) because it is the method that the entity expects to better predict the amount of consideration to which it will be entitled. Using the expected value method, the entity estimates that 970 products will not be returned.

Step 3:

Determine the transaction price Overview

Solution

The entity recognises revenue of Rs. 10,000 ($10 \text{ units} \times \text{Rs. } 1,000 \text{ per unit}$) for the quarter ended 30 June 20X1. HT Limited recognises revenue of Rs. 44,000 for the quarter ended 30 September 20X1. That amount is calculated from Rs. 45,000 for the sale of 500 units ($50 \text{ units} \times \text{Rs. } 900 \text{ per unit}$) less the change in transaction price of Rs. 1,000 ($10 \text{ units} \times \text{Rs. } 100 \text{ price reduction}$) for the reduction of revenue relating to units sold for the quarter ended 30 June 20X1.

Step 3:

Determine the transaction price Overview

Example(Cont.)

The entity estimates that the costs of recovering the products will be immaterial and expects that the returned products can be resold at a profit.

Determine the amount of revenue, refund liability and the asset to be recognised by the entity for the said contracts.

Step 3:

Determine the transaction price Overview

Solution

The entity also considers the requirements in paragraphs 56–58 of Ind AS 115 on constraining estimates of variable consideration to determine whether the estimated amount of variable consideration of Rs. 48,500 (Rs. 50 × 970 products not expected to be returned) can be included in the transaction price. The entity considers the factors in paragraph 57 of Ind AS 115 and determines that although the returns are outside the entity's influence, it has significant experience in estimating returns for this product and customer class. In addition, the uncertainty will be resolved within a short time frame (ie the 30-day return period). Thus, the entity concludes that it is highly probable that a significant reversal in the cumulative amount of revenue recognised (i.e. Rs. 48,500) will not occur as the uncertainty is resolved (i.e. over the return period).

The entity estimates that the costs of recovering the products will be immaterial and expects that the returned products can be resold at a profit.

Upon transfer of control of the 1,000 products, the entity does not recognise revenue for the 30 products that it expects to be returned. Consequently, in accordance with paragraphs 55 and B21 of Ind AS 115, the entity recognises the following:

- (a) revenue of Rs. 48,500 (Rs. 50 × 970 products not expected to be returned);
- (b) a refund liability of Rs. 1,500 (Rs. 50 refund × 30 products expected to be returned); and
- (c) an asset of Rs. 900 (Rs. 30 × 30 products for its right to recover products from customers on settling the refund liability).

Step 3:

Determine the transaction price Overview

Example

On 1 April 20X1, an entity enters into a contract with a client to provide asset management services for five years. The entity receives a two per cent quarterly management fee based on the client's assets under management at the end of each quarter. At 31 March 20X2, the client's assets under management are Rs. 100 crores. In addition, the entity receives a performance-based incentive fee of 20 per cent of the fund's return in excess of the return of an observable market index over the five-year period. Consequently, both the management fee and the performance fee in the contract are variable consideration. Analyse the revenue to be recognised on 31 March, 20X2.

Step 3:

Determine the transaction price Overview

Solution

The entity accounts for the services as a single performance obligation because it is providing a series of distinct services that are substantially the same and have the same pattern of transfer (the services transfer to the customer over time and use the same method to measure progress—that is, a time-based measure of progress).

The entity observes that the promised consideration is dependent on the market and thus is highly susceptible to factors outside the entity's influence. In addition, the incentive fee has a large number and a broad range of possible consideration amounts. The entity also observes that although it has experience with similar contracts, that experience is of little predictive value in determining the future performance of the market. Therefore, at contract inception, the entity cannot conclude that it is highly probable that a significant reversal in the cumulative amount of revenue recognised would not occur if the entity included its estimate of the management fee or the incentive fee in the transaction price. At each reporting date, the entity updates its estimate of the transaction price. Consequently, at the end of each quarter, the entity concludes that it can include in the transaction price the actual amount of the quarterly management fee because the uncertainty is resolved. However, the entity concludes that it cannot include its estimate of the incentive fee in the transaction price at those dates.

Step 3:

Determine the transaction price Overview

Solution(Cont.)

This is because there has not been a change in its assessment from contract inception—the variability of the fee based on the market index indicates that the entity cannot conclude that it is highly probable that a significant reversal in the cumulative amount of revenue recognised would not occur if the entity included its estimate of the incentive fee in the transaction price.

At 31 March 20X2, the client's assets under management are Rs. 100 crores. Therefore, the resulting quarterly management fee and the transaction price is Rs. 2 crores.

At the end of each quarter, the entity allocates the quarterly management fee to the distinct services provided during the quarter. This is because the fee relates specifically to the entity's efforts to transfer the services for that quarter, which are distinct from the services provided in other quarters.

Consequently, the entity recognises Rs. 2 crores as revenue for the quarter ended 31 March 20X2.

Step 3:

Determine the transaction price Overview

Warranties

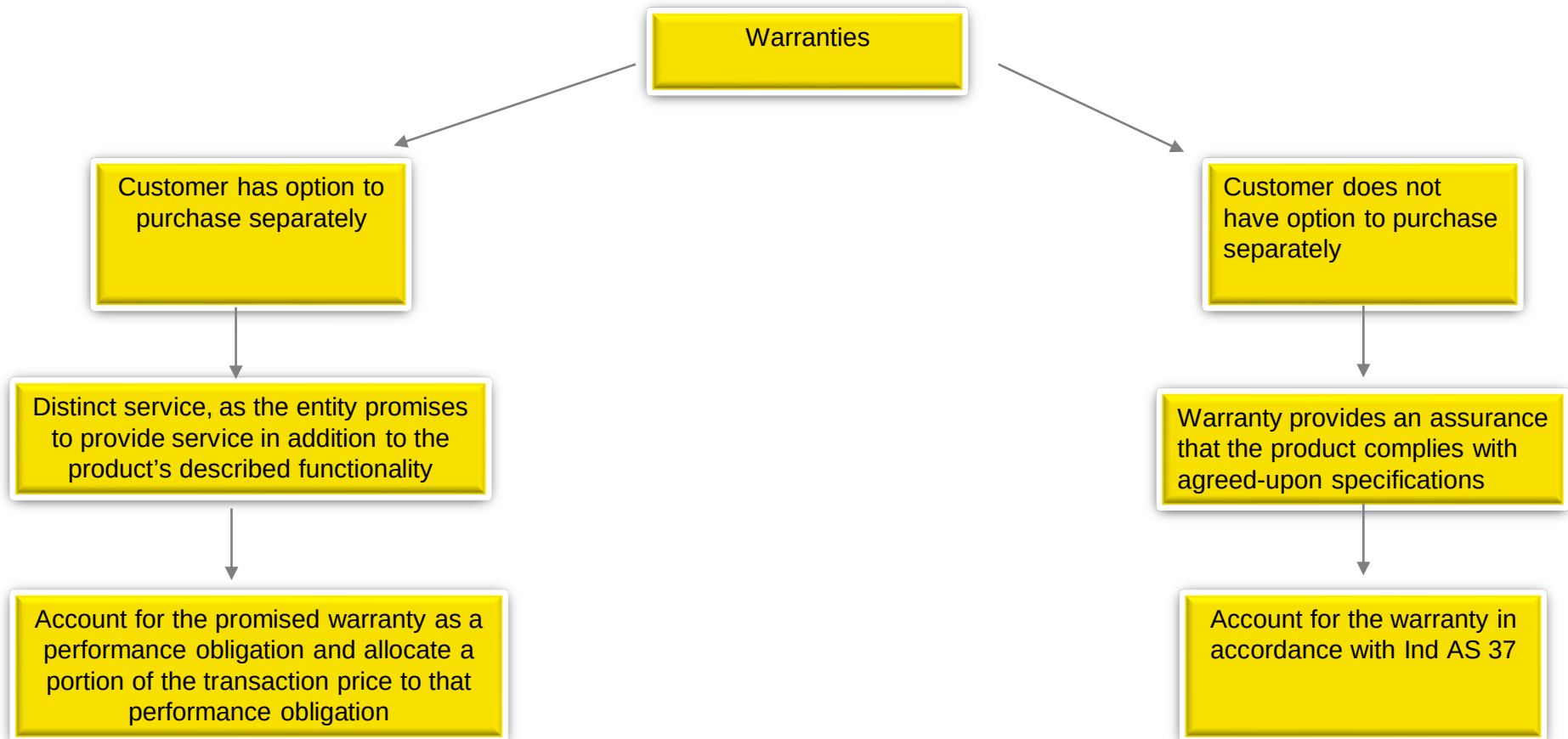
It is common for an entity to provide (in accordance with the contract, the law or the entity's customary business practices) a warranty in connection with the sale of a product (whether a good or service). The nature of a warranty can vary significantly across industries and contracts.

Some warranties provide a customer with assurance that the related product will function as the parties intended because it complies with agreed-upon specifications. Other warranties provide the customer with a service in addition to the assurance that the product complies with agreed-upon specifications.

Step 3:

Determine the transaction price Overview

Warranties(Cont.)



Step 3:

Determine the transaction price Overview

Sales-based or usage-based royalties

As per Ind AS 115.B63, notwithstanding the requirements of Ind AS 115 related to constraining estimate of variable consideration (discussed above), an entity shall recognise revenue for a sales-based or usage-based royalty promised in exchange for a licence of intellectual property only when (or as) the later of the following events occurs:

- (a) the subsequent sale or usage occurs; and
- (b) the performance obligation to which some or all of the sales-based or usage-based royalty has been allocated has been satisfied (or partially satisfied).

As per Ind AS 115.B63A, the accounting requirements for a sales-based or usage-based royalty discussed above apply when the royalty relates only to a licence of intellectual property or when a licence of intellectual property is the predominant item to which the royalty relates (for example, the licence of intellectual property may be the predominant item to which the royalty relates when the entity has a reasonable expectation that the customer would ascribe significantly more value to the licence than to the other goods or services to which the royalty relates).

As per Ind AS 115.B63B, when the requirement in paragraph B63A is met, revenue from a sales-based or usage-based royalty shall be recognised wholly in accordance with paragraph B63. When the requirement in paragraph B63A is not met, the requirements on variable consideration discussed earlier apply to the sales-based or usage-based royalty.

Step 3:

Determine the transaction price

Significant financing component

Time value of money



An entity adjusts the transaction price for the effects of the time value of money if the timing of the payments provides either party with a significant benefit of financing



Evaluation not required if the entity expects the period between transfer of performance obligations and receipt of payment is one year or less



If the financing component is not significant to the individual contract, entity is not required to adjust the transaction price

When assessing significance, entity would consider:



The difference between promised consideration and the cash selling price

Combined effect of:



Expected time between transfer of the promised goods and services and payment from customer



Prevailing interest rates in the relevant market

Step 3:

Determine the transaction price

Significant financing component

A contract would not have a significant financing component if any of the following factors exists:



The customer paid in advance and the timing of the transfer of promised goods or services is at the discretion of the customer



A substantial amount of the consideration is variable, and the amount or timing varies based on a future event that is not substantially within the control of the customer or the entity



The difference between the promised consideration and the cash selling price arises for reasons other than the provision of finance to either the customer or the entity, and the amount of the difference is proportional to the reason for the difference

- ▶ This indicator requires significant judgement
- ▶ Examples in the standard include protection from risk of non-performance

Step 3:

Determine the transaction price Overview

Example

A commercial airplane component supplier enters into a contract with a customer for promised consideration of Rs. 7,000,000. Based on an evaluation of the facts and circumstances, the supplier concluded that Rs. 140,000 represented a insignificant financing component because of an advance payment received in excess of a year before the transfer of control of the product.

State whether company needs to make any adjustment in determining the transaction price. What if the advance payment was larger and received further in advance, such that the entity concluded that Rs. 1,400,000 represented the financing component based on an analysis of the facts and circumstances.

Step 3:

Determine the transaction price Overview

Solution

The entity may conclude that Rs. 140,000, or 2 percent of the contract price, is not significant, and the entity may not need to adjust the consideration promised in determining the transaction price.

However, when the advance payment was larger and received further in advance, such that the entity may conclude that Rs. 1,400,000 represents the financing component based on an analysis of the facts and circumstances. In such a case, the entity may conclude that Rs. 1,400,000, or 20 percent of the contract price, is significant, and the entity should adjust the consideration promised in determining the transaction price.

Note: In this illustration, the entity's conclusion that 2 percent of the transaction price was not significant and 20 percent was significant is a judgment based on the entity's facts and circumstances. An entity may reach a different conclusion based on its facts and circumstances.

Step 3:

Determine the transaction price Overview

Example

NKT Limited sells a product to a customer for Rs. 121,000 that is payable 24 months after delivery. The customer obtains control of the product at contract inception. The contract permits the customer to return the product within 90 days. The product is new and the entity has no relevant historical evidence of product returns or other available market evidence.

The cash selling price of the product is Rs. 100,000 which represents the amount that the customer would pay upon delivery for the same product sold under otherwise identical terms and conditions as at contract inception. The entity's cost of the product is Rs. 80,000. The contract includes an implicit interest rate of 10 per cent (i.e. the interest rate that over 24 months discounts the promised consideration of Rs. 121,000 to the cash selling price of Rs. 100,000).

Analyse the above transaction with respect to its financing component.

Step 3:

Determine the transaction price Overview

Solution

The contract includes a significant financing component. This is evident from the difference between the amount of promised consideration of Rs. 121,000 and the cash selling price of Rs. 100,000 at the date that the goods are transferred to the customer.

The contract includes an implicit interest rate of 10 per cent (i.e. the interest rate that over 24 months discounts the promised consideration of Rs. 121,000 to the cash selling price of Rs. 100,000). The entity evaluates the rate and concludes that it is commensurate with the rate that would be reflected in a separate financing transaction between the entity and its customer at contract inception.

Until the entity receives the cash payment from the customer, interest revenue would be recognised in accordance with Ind AS 109. In determining the effective interest rate in accordance with Ind AS 109, the entity would consider the remaining contractual term.

Step 3:

Determine the transaction price Overview

Example

VT Limited enters into a contract with a customer to sell equipment. Control of the equipment transfers to the customer when the contract is signed. The price stated in the contract is Rs. 1 crore plus a 10% contractual rate of interest, payable in 60 monthly instalments of Rs. 212,470.

Determine the discounting rate and the transaction price when

Case A—Contractual discount rate reflects the rate in a separate financing transaction

Case B—Contractual discount rate does not reflect the rate in a separate financing transaction ie 14%.

Step 3:

Determine the transaction price Overview

Solution-Case A

In evaluating the discount rate in the contract that contains a significant financing component, VT Limited observes that the 10% contractual rate of interest reflects the rate that would be used in a separate financing transaction between the entity and its customer at contract inception (i.e. the contractual rate of interest of 10% reflects the credit characteristics of the customer).

The market terms of the financing mean that the cash selling price of the equipment is Rs. 1 crore. This amount is recognised as revenue and as a loan receivable when control of the equipment transfers to the customer. The entity accounts for the receivable in accordance with Ind AS 109.

Step 3:

Determine the transaction price Overview

Solution-Case B

In evaluating the discount rate in the contract that contains a significant financing component, the entity observes that the 10% contractual rate of interest is significantly lower than the 14% interest rate that would be used in a separate financing transaction between the entity and its customer at contract inception (i.e. the contractual rate of interest of 10% does not reflect the credit characteristics of the customer). This suggests that the cash selling price is less than Rs. 1 crore.

VT Limited determines the transaction price by adjusting the promised amount of consideration to reflect the contractual payments using the 14% interest rate that reflects the credit characteristics of the customer. Consequently, the entity determines that the transaction price is Rs. 9,131,346 (60 monthly payments of Rs. 212,470 discounted at 14%). The entity recognises revenue and a loan receivable for that amount. The entity accounts for the loan receivable in accordance with Ind AS 109.

Step 3:

Determine the transaction price Overview

Example

ST Limited enters into a contract with a customer to sell an asset. Control of the asset will transfer to the customer in two years (i.e. the performance obligation will be satisfied at a point in time). The contract includes two alternative payment options:

- 1) Payment of Rs. 5,000 in two years when the customer obtains control of the asset or
- 2) Payment of Rs. 4,000 when the contract is signed. The customer elects to pay Rs. 4,000 when the contract is signed.

ST Limited concludes that the contract contains a significant financing component because of the length of time between when the customer pays for the asset and when the entity transfers the asset to the customer, as well as the prevailing interest rates in the market.

The interest rate implicit in the transaction is 11.8 per cent, which is the interest rate necessary to make the two alternative payment options economically equivalent. However, the entity determines that, the rate that should be used in adjusting the promised consideration is 6%, which is the entity's incremental borrowing rate.

Pass journal entries showing how the entity would account for the significant financing component

Step 3:

Determine the transaction price

Solution

Journal Entries showing accounting for the significant financing component:

(a) Recognise a contract liability for the Rs. 4,000 payment received at contract inception:

Cash	Dr.	Rs. 4,000	
	To Contract liability		Rs. 4,000

(b) During the two years from contract inception until the transfer of the asset, the entity adjusts the promised amount of consideration and accretes the contract liability by recognising interest on Rs. 4,000 at 6% for two years:

Interest expense	Dr.	Rs. 494*	
	To Contract liability		Rs. 494

* Rs. 494 = Rs. 4,000 contract liability × (6% interest per year for two years).

(c) Recognise revenue for the transfer of the asset:

Contract liability	Dr.	Rs. 4,494	
	To Revenue		Rs. 4,494

Step 3:

Determine the transaction price

Example

ABC Limited enters into a contract for the construction of a power plant that includes scheduled milestone payments for the performance by ABC Limited throughout the contract term of three years. The performance obligation will be satisfied over time and the milestone payments are scheduled to coincide with the expected performance by ABC Limited. The contract provides that a specified percentage of each milestone payment is to be withheld as retention money by the customer throughout the arrangement and paid to the entity only when the building is complete. Analyse whether the contract contains any financing component.

Step 3:

Determine the transaction price

Solution

ABC Limited concludes that the contract does not include a significant financing component since the milestone payments coincide with its performance and the contract requires amounts to be retained for reasons other than the provision of finance. The withholding of a specified percentage of each milestone payment is intended to protect the customer from the contractor failing to adequately complete its obligations under the contract.

Step 3:

Determine the transaction price

Example

XYZ Limited, a personal computer (PC) manufacturer, enters into a contract with a customer to provide global PC support and repair coverage for three years along with its PC. The customer purchases this support service at the time of buying the product. Consideration for the service is an additional Rs. 3,000. Customers electing to buy this service must pay for it upfront (i.e. a monthly payment option is not available).

Analyse whether there is any significant financing component in the contract or not.

Step 3:

Determine the transaction price

Solution

To determine whether there is a significant financing component in the contract, the entity considers the nature of the service being offered and the purpose of the payment terms. The entity charges a single upfront amount, not with the primary purpose of obtaining financing from the customer but, instead, to maximise profitability, taking into consideration the risks associated with providing the service.

Specifically, if customers could pay monthly, they would be less likely to renew and the population of customers that continue to use the support service in the later years may become smaller and less diverse over time (i.e. customers that choose to renew historically are those that make greater use of the service, thereby increasing the entity's costs). In addition, customers tend to use services more if they pay monthly rather than making an upfront payment. Finally, the entity would incur higher administration costs such as the costs related to administering renewals and collection of monthly payments.

In assessing whether or not the contract contains a significant financing component, XYZ Limited determines that the payment terms were structured primarily for reasons other than the provision of finance to the entity. XYZ Limited charges a single upfront amount for the services because other payment terms (such as a monthly payment plan) would affect the nature of the risks it assumes to provide the service and may make it uneconomical to provide the service. As a result of its analysis, XYZ Limited concludes that there is not a significant financing component.

Step 3:

Determine the transaction price

Example

A computer hardware vendor enters into a three-year arrangement with a customer to provide support services. For customers with low credit ratings, the vendor requires the customer to pay for the entire arrangement in advance of the provision of service. Other customers pay over time. Analyse whether there is any significant financing component in the contract or not.

Step 3:

Determine the transaction price

Solution

Due to this customer's credit rating, the customer pays in advance for the three -year term. Because there is no difference between the amount of promised consideration and the cash selling price (that is, the customer does not receive a discount for paying in advance), the vendor requires payment in advance only to protect against customer non-payment, and no other factors exist to suggest the arrangement contains a financing, the vendor concludes this contract does not provide the customer or the entity with a significant benefit of financing.

Step 3:

Determine the transaction price

Example

A software vendor enters into a contract with a customer to provide a license solely in exchange for a sales-based royalty.

Analyse whether there is any significant financing component in the contract or not.

Step 3:

Determine the transaction price

Solution

Although the payment will be made in arrears, because the total consideration varies based on the occurrence or non-occurrence of a future event that is not within the control of the customer or the entity, the software vendor concludes the contract does not provide the customer or the entity with a significant benefit of financing.

Step 3:

Determine the transaction price

Example

An EPC contractor enters into a two-year contract to develop customized machine for a customer. The contractor concludes that the goods and services in this contract constitute a single performance obligation.

Based on the terms of the contract, the contractor determines that it transfers control over time, and recognizes revenue based on an input method best reflecting the transfer of control to the customer. The customer agrees to provide the contractor monthly progress payments, with the final 25 percent payment (holdback payment) due upon contract completion. As a result of the holdback payment, there is a gap between when control transfers and when consideration is received, creating a financing component. Analyse whether there is any significant financing component in the contract or not.

Step 3:

Determine the transaction price

Solution

There is no difference between the amount of promised consideration and the cash selling price (that is, the customer did not pay a premium for paying a portion of the consideration in arrears). The payment terms included a holdback payment only to ensure successful completion of the project, and no other factors exist to suggest the arrangement contains a financing . Hence, the contractor concludes this contract does not provide the customer or the contractor with a significant benefit of financing.

Step 3:

Determine the transaction price

Example

Company Z is a developer and manufacturer of defence systems that is primarily a Tier-II supplier of parts and integrated systems to original equipment manufacturers (OEMs) in the commercial markets. Company Z enters into a contract with Company X for the development and delivery of 5,000 highly technical, specialized missiles for use in one of Company X's platforms.

As a part of the contract, Company X has agreed to pay Company Z for their cost plus an award fee up to Rs. 100 crores. The consideration will be paid by the customer related to costs incurred near the time Company Z incurs such costs. However, the Rs. 100 crores award fee is awarded upon successful completion of the development and test fire of a missile to occur in 16 months from the time the contract is executed.

The contract specifies Company Z will earn up to Rs. 100 crores based on Company X's assessment of Company Z's ability to develop and manufacture a missile that achieves multiple factors, including final weight, velocity, and accuracy. Partial award fees may be awarded based on a pre-determined scale based on their success.

Assume Company Z has assessed the contract under Ind AS 115 and determined the award fee represents variable consideration. Based on their assessment, Company Z has estimated a total of Rs. 80 crores in the transaction price related to the variable consideration pursuant to guidance within Ind AS 115. Further, the entity has concluded it should recognize revenue over time for a single performance obligation using a cost-to-cost input method.

Analyse whether there is any significant financing component in the contract or not.

Step 3:

Determine the transaction price

Solution

Company Z will transfer control over time beginning shortly after the contract is executed, but will not receive the cash consideration related to the award fee component from Company X for more than one year in the future. Hence, Company Z should assess whether the award fee represents a significant financing component.

The intention of the parties in negotiating the award fee due upon completion of the test fire, and based on the results of that test fire, was to provide incentive to Company Z to produce high functioning missiles that achieved successful scoring from Company X. Therefore, it was determined the contract does not contain a significant financing component, and Company Z should not adjust the transaction price.

As per Ind AS 115.63, as a practical expedient, an entity need not adjust the promised amount of consideration for the effects of a significant financing component if the entity expects, at contract inception, that the period between:

- (a) when the entity transfers a promised good or service to a customer and
- (b) when the customer pays for that good or service will be one year or less.

Step 3:

Determine the transaction price

Example

Company H enters into a two-year contract to develop customized software for Company C. Company H concludes that the goods and services in this contract constitute a single performance obligation.

Based on the terms of the contract, Company H determines that it transfers control over time, and recognizes revenue based on an input method best reflecting the transfer of control to Company C.

Company C agrees to provide Company H monthly progress payments. Based on the expectation of the timing of costs to be incurred, Company H concludes that progress payments are being made such that the timing between the transfer of control and payment is never expected to exceed one year.

Analyse whether there is any significant financing component in the contract or not.

Step 3:

Determine the transaction price

Solution

Company H concludes it will not need to further assess whether a significant financing component is present and does not adjust the promised consideration in determining the transaction price, as they are applying the practical expedient under Ind AS 115.

As per Ind AS 115.65, an entity shall present the effects of financing (interest revenue or interest expense) separately from revenue from contracts with customers in the statement of profit and loss. Interest revenue or interest expense is recognised only to the extent that a contract asset (or receivable) or a contract liability is recognised in accounting for a contract with a customer.

Step 3:

Determine the transaction price

Non-cash consideration

Measured at the fair value

When an entity expects to receive non-cash consideration, such consideration is measured at the fair value of the amounts received or promised and is included in the transaction price

Reference to the selling price

If the fair value cannot be reliably estimated, non-cash consideration is to be measured indirectly by reference to the selling price of the goods or services transferred to the customer



If the non-cash consideration promised is variable for reasons other than just the form of non-cash consideration, the constraint on variable consideration should be applied.

For example, the constraint would not be applied to consider changes in the fair value of stock to be received as non-cash consideration

Step 3:

Determine the transaction price

Example

An entity enters into a contract with a customer to provide a weekly service for one year. The contract is signed on 1st April 20X1 and work begins immediately. The entity concludes that the service is a single performance obligation. This is because the entity is providing a series of distinct services that are substantially the same and have the same pattern of transfer (the services transfer to the customer over time and use the same method to measure progress — that is, a time-based measure of progress).

In exchange for the service, the customer promises its 100 equity shares per week of service (a total of 5,200 shares for the contract). The terms in the contract require that the shares must be paid upon the successful completion of each week of service. How should the entity decide the transaction price?

Step 3:

Determine the transaction price

Solution

The entity measures its progress towards complete satisfaction of the performance obligation as each week of service is complete. To determine the transaction price (and the amount of revenue to be recognised), the entity has to measure the fair value of 100 shares that are received upon completion of each weekly service. The entity shall not reflect any subsequent changes in the fair value of the shares received (or receivable) in revenue.

Step 3:

Determine the transaction price

Example

RT Limited enters into a contract to build an office building for AT Limited over an 18-month period. AT Limited agrees to pay the construction entity Rs. 350 crores for the project. RT Limited will receive a bonus of 10 lakhs equity shares of AT Limited if it completes construction of the office building within one year. Assume a fair value of Rs. 100 per share at contract inception. Determine the transaction price.

Step 3:

Determine the transaction price

Solution

The ultimate value of any shares the entity might receive could change for two reasons:

- 1) the entity earns or does not earn the shares and
- 2) the fair value per share may change during the contract term.

When determining the transaction price, the entity would reflect changes in the number of shares to be earned. However, the entity would not reflect changes in the fair value per share. Said another way, the share price of Rs. 100 is used to value the potential bonus throughout the life of the contract.

As a result, if the entity earns the bonus, its revenue would be Rs. 350 crores plus 10 lakhs equity shares at Rs. 100 per share for total consideration of Rs. 360 crores.

Step 3:

Determine the transaction price

Customer-provided goods or services

If a customer contributes goods or services (for example, materials, equipment or labour) to facilitate an entity's fulfilment of the contract, the entity shall assess whether it obtains control of those contributed goods or services. If so, the entity shall account for the contributed goods or services as non-cash consideration received from the customer.

Step 3:

Determine the transaction price

Example

MS Limited is a manufacturer of cars. It has a supplier of steering systems – SK Limited. MS Limited places an order of 10,000 steering systems on SK Limited. It also agrees to pay Rs. 25,000 per steering system and contributes tooling to be used in SK's production process.

The tooling has a fair value of Rs. 2 crores at contract inception. SK Limited determines that each steering system represents a single performance obligation and that control of the steering system transfers to MS Limited upon delivery.

SK Limited may use the tooling for other projects and determines that it obtains control of the tooling. Determine the transaction price?

Step 3:

Determine the transaction price

Solution

As a result, at contract inception, SK Limited includes the fair value of the tooling in the transaction price at contract inception, which it determines to be Rs. 27 crores (Rs. 25 crores for the steering systems and Rs. 2 crores for the tooling).

Step 3:

Determine the transaction price

Consideration paid or payable to a customer

Entity determines whether amounts paid or payable to the customer (e.g., cash, credit) are:



A reduction of the transaction price and revenue



A payment for distinct goods and services



A combination of the two

Distinct goods or services

For an entity to treat the consideration paid or payable to a customer as something other than a reduction of revenue, the goods or services from the customer must be 'distinct'

Reductions to the transaction price occur at the later of when:

The entity recognises revenue for the transfer of control of the goods or services to the customer

The entity pays or promises to pay the consideration

Step 3:

Determine the transaction price

Consideration paid or payable to a customer – Example

- ▶ Entity A enters into a contract with a customer for the exclusive supply of paint for a three-year period
- ▶ Entity A makes a CU50,000 upfront payment, which the customer will use to customise its paint sprayers for Entity A's product
- ▶ Entity A determines the upfront payment is not a distinct good or service
 - ▶ CU50,000 to be accounted for as a reduction of the transaction price
 - ▶ Entity A estimates CU1,000,000 in sales with the customer over the three-year period
- ▶ The upfront payment is deferred and recognised as a reduction of revenue (in proportion to estimated sales) over the contract term

Step 3:

Determine the transaction price

Consideration paid or payable to a customer – Example

For the first quarter

- ▶ Q1 sales = CU100,000
- ▶ Entity A continues to estimate CU1M in sales
- ▶ $\text{CU100,000} / \text{CU1.0M} = 10\%$ of estimated sales
- ▶ $10\% \times \text{CU50,000}$ upfront payment = CU5,000 to be recognised in Q1
- ▶ Entity A recognises revenue of CU95,000
(CU100,000 actual sales - CU5,000 portion of consideration paid to the customer)

For the first quarter

- ▶ Q2 sales = CU125,000
- ▶ Entity A updates its estimates of total sales over the contract to CU1.5M
- ▶ CU225,000 total sales to date / CU1.5M estimated total sales = 15%
- ▶ $15\% \times \text{CU50,000}$ upfront payment = CU7,500 - CU5,000 recognised in Q1 = CU2,500 to be recognised in Q2
- ▶ Entity A recognises revenue of CU122,500 for Q2
(CU125,000 actual sales - CU2,500 portion of consideration paid to the customer)

Step 3:

Determine the transaction price

Example

An entity that manufactures consumer goods enters into a one-year contract to sell goods to a customer that is a large global chain of retail stores. The customer commits to buy at least Rs. 15 crores of products during the year. The contract also requires the entity to make a non-refundable payment of Rs. 1.5 crores to the customer at the inception of the contract. The Rs. 1.5 crores payment will compensate the customer for the changes it needs to make to its shelving to accommodate the entity's products. The entity does not obtain control of any rights to the customer's shelves.

Determine the transaction price.

Step 3:

Determine the transaction price

Consideration paid or payable to a customer – Example

The entity considers the requirements in paragraphs 70 – 72 of Ind AS 115 and concludes that the payment to the customer is not in exchange for a distinct good or service that it transfers to the entity. This is because the entity does not obtain control of any rights to the customer's shelves. Consequently, the entity determines that, in accordance with paragraph 70 of Ind AS 115, the Rs. 1.5 crores payment is a reduction of the transaction price.

The entity applies the requirements in paragraph 72 of Ind AS 115 and concludes that the consideration payable is accounted for as a reduction in the transaction price when the entity recognises revenue for the transfer of the goods. Consequently, as the entity transfers goods to the customer, the entity reduces the transaction price for each good by 10 per cent $[(Rs. 1.5 \text{ crores} \div Rs. 15 \text{ crores}) \times 100]$. Therefore, in the first month in which the entity transfers goods to the customer, the entity recognises revenue of Rs. 1.125 crores (Rs. 1.25 crores invoiced amount less Rs. 0.125 crore of consideration payable to the customer).

Step 3:

Determine the transaction price

Non-refundable upfront fees



Entities may receive payments from customers before goods or services are provided, e.g., joining fees for health club membership, activation fees for telecommunication contracts, set-up fees etc.



In many cases, upfront payments are non-refundable



Entities must evaluate whether non-refundable upfront fees relate to the transfer of a (future) good or service

Set-up activities



Fees charged for set-up activities – these activities do not depict the transfer of services to a customer and should be ignored when measuring progress of an entity's performance



The existence of a non-refundable upfront fee may indicate the arrangement includes an option for additional goods or services (e.g., renewal option for future goods or services at a reduced price)

Step 3:

Determine the transaction price

Variable consideration- Example 1

- ▶ Entity enters into a contract and will receive a INR100,000 performance bonus if specified performance targets are met
- ▶ Entity estimates 80% likelihood it will receive entire performance bonus and 20% likelihood it will receive none of the bonus

Conclusion

Due to the binary nature of the outcome, Entity determines that the best predictor of the ultimate consideration it will receive is the 'most likely amount' approach.

Therefore, INR100,000 is included in the transaction price

Constraint likely has no effect because Entity concludes it is probable that the bonus will be received

Step 3:

Determine the transaction price

Variable consideration- Example 2

Entity enters into a contract and will receive a performance bonus up to INR100,000 if it meets specified performance targets. It estimates the likelihood of achieving the targets as:

Possible outcomes	Probability	Calculated amount
INR100,000	10%	INR10,000
INR80,000	30%	INR24,000
INR60,000	35%	INR21,000
INR40,000	10%	INR4,000
-	15%	-
		INR59,000

‘Expected value’ approach is determined to be the best method, Entity calculates INR59,000 using this method

However, Entity must consider whether any of the INR59,000 needs to be constrained.

Step 3:

Determine the transaction price

Variable consideration- Example 3

Entity enters into a contract and will receive a performance bonus based on five potential amounts if specified targets are met. It estimates the likelihood of achieving the targets, as follows:

Possible outcomes	Probability	Calculated amount
CU100,000	15%	CU15,000
CU80,000	30%	CU24,000
CU60,000	30%	CU18,000
CU40,000	10%	CU4,000
-	15%	-
		CU61,000

‘Expected value’ approach is determined to be the best method, Entity calculates INR61,000 using this method . Constraint limits bonus to INR60,000 until it is probable that the next bonus level will be achieved

Step 3:

Determine the transaction price

Variable consideration- Example 4

- ▶ Company A supplies components to industrial customers.
- ▶ The contract stipulates that price per component will decrease as sales volume increases within the stipulated period of time.
- ▶ The price applicable for the entire sale will be based on sales volume bracket.

Price per unit	Sales volume
CU100	0 -1,000,000 units
CU90	1,000,000 - 3,000,000 units
CU85	3,000,001 units and above

How is revenue estimated under Ind AS 115?

Step 3:

Determine the transaction price

Variable consideration- Expected Value

- ▶ A estimates probability-weighted variable consideration based on the range of possible outcomes and probabilities of each outcome.
- ▶ All possible outcomes are required to be assessed and quantified

Probability	Sales volume (units)	Price/ unit (Rs.)	Probability-weighted sales value (Rs.)	Probability-weighted sales volume (units)
10%	800,000 units	100	8,000,000	80,000
70%	2,500,000 units	90	157,500,000	1,750,000
20%	3,500,000 units	85	59,500,000	700,000
			A= 225,000,000	B= 2,530,000

- ▶ Avg unit price = Rs.88.93 (A/B). Revenue is recognised at Rs.88.93 for each unit sold. For the first 1,000,000 units sold, liability is accrued at Rs.11.07 (100-88.93) per unit, reversed upon subsequent sales.

Step 3:

Determine the transaction price

Variable consideration- Most likely approach

- ▶ Consider the following change in fact pattern:

A believes that the total sales volume for the year will be 2.5 million based on past experience and forecasted sales.

- ▶ Based on the most likely method, the transaction price is calculated as follows:

Rs.90 per unit X 2,500,000 units

Rs. 225,000,000

- ▶ Average unit price = Rs.90
- ▶ Revenue is recognised at 90 per unit for each unit sold.
- ▶ For the first 1,000,000 units sold, liability is accrued at Rs.10(100-90) per unit.

Step 3:

Practical challenges

If a contract is denominated in a currency other than that of the entity's functional currency, should changes in the contract price due to exchange rate fluctuations be accounted for as variable consideration?

- ▶ These price fluctuations are a consequence of entering into a contract that is denominated in a foreign currency, rather than a result of a contract term like a discount or rebate or one that depends on the occurrence or non-occurrence of a future event. The variability resulting from changes in foreign exchange rates relates to the **form of the consideration** and it would not be considered variable consideration when determining the transaction price. This variability may, instead, need to be accounted for in accordance with Ind AS 109 (if it is a separable embedded derivative) or as per Ind AS 21.

How should an entity account for restocking fees for goods that are expected to be returned?

- ▶ Restocking fees for goods that are expected to be returned would be included in **the estimate of the transaction price** at contract inception and recorded as revenue when (or as) control of the good transfers.

Step 3:

Case study 1

Facts

- ▶ Entity A enters into a contract with a distributor (its customer) and transfers control of 1,000 products at contract inception for consideration of CU100 per product.
- ▶ Payment from the distributor is due when the distributor sells the products to the end consumer, which generally occurs within 90 days of obtaining control of the products.
- ▶ To maintain its relationship with the distributor and based on past practices, Entity A anticipates granting a price concession in order to help the distributor move the product through the distribution chain.
- ▶ As a result, the consideration in the contract is variable.
- ▶ Entity A has significant experience selling this and similar products.
- ▶ Data shows that a 20% price concession has historically been granted.
- ▶ Current market information suggests that a 20% price concession will be sufficient to move the products through the distribution chain.

Apply the requirements for variable consideration and the constraint to this scenario.

Step 3:

Case study 1 – Scenario A

Analysis and conclusion

Estimate the variable consideration

Entity A uses an expected value method to estimate the transaction price to be CU80,000 (CU80 x 1,000 products).

Evaluate whether it needs to constrain any of this estimated amount, including consideration of the constraint factors in paragraph 57 of Ind AS 115

Entity A uses an expected value method to estimate the transaction price to be CU80,000 (CU80 x 1,000 products).

- ▶ Conclusion: Based on its specific facts and circumstances, Entity A concludes that it is highly probable that a significant reversal of cumulative revenue will not occur if it includes CU80,000 in the transaction price.
- ▶ Entity A recognises CU80,000 in revenue when the products are transferred to the distributor at contract inception.

Step 3:

Case study 2 Facts

- ▶ An entity sells a product to a customer for CU121 that is payable 24 months after delivery
- ▶ The customer obtains control of the product at contract inception
- ▶ The cash selling price of the product at contract inception is CU100
- ▶ Initial journal entry (ignoring cost of sales):

DR	Receivable	CU100	
	CR	Revenue	CU100

Is there a significant financing component?

Step 3:

Case study 2 – Scenario A

Analysis and conclusion

- ▶ The contract includes a significant financing component, as evident from the difference between the amount of promised consideration of CU121 and the cash selling price of CU100 at the date that the goods are transferred to the customer.
 - ▶ Until the entity receives the cash payment from the customer, interest income would be recognised consistent with requirements in Ind AS 109 *Financial Instruments*.
 - ▶ The entity would accrete the receivable up to CU121 from the time that control transfers of the good until the time that the customer pays.
 - ▶ The contract includes an implicit interest rate of 10% (i.e., the interest rate that over 24 months discounts the promised consideration of CU121 to the cash selling price of CU100).
 - ▶ The entity evaluates the rate and concludes that it is commensurate with the rate that would be reflected in a separate financing transaction between the entity and its customer at contract inception.

Step 3:

Determine the transaction price Overview

Penalties

As per Ind AS 115.51AA, penalties shall be accounted for as per the substance of the contract.

Where the penalty is inherent in determination of transaction price, it shall form part of variable consideration.

For example, where an entity agrees to transfer control of a good or service in a contract with customer at the end of 30 days for Rs. 100,000 and if it exceeds 30 days, the entity is entitled to receive only Rs. 95,000, the reduction of Rs. 5,000 shall be regarded as variable consideration. In other cases, the transaction price shall be considered as fixed.

Step 4: Allocate the transaction price to the performance obligations in the contract

Step 4:

Allocate the transaction price

Allocate based on relative stand-alone selling prices

Performance obligation 1

Performance obligation 2

Performance obligation 3

Determine stand-alone selling prices

Is observable price available?

Yes

Use observable price

Exceptions to the allocation requirement:

- ▶ Variable consideration

No

Estimate price

Adjusted market
assessment approach

Expected cost plus a
margin

Residual approach

Step 4:

Allocate the transaction price

Allocation of a discount

A customer receives a discount for purchasing a bundle of goods or services if the sum of the stand-alone selling prices of those promised goods or services in the contract exceeds the promised consideration in a contract.

Unless an entity has observable evidence (if (c) criteria below are fulfilled) that the entire discount relates to only one or more, but not all, performance obligations in a contract, the entity shall allocate a discount proportionately to all performance obligations in the contract. The proportionate allocation of the discount in those circumstances is a consequence of the entity allocating the transaction price to each performance obligation on the basis of the relative stand-alone selling prices of the underlying distinct goods or services (as discussed earlier).

Step 4:

Allocate the transaction price

Allocation of a discount

When to allocate discount to 'less than all' performance obligations?

As per Ind AS 115.82, an entity shall allocate a discount entirely to one or more, but not all, performance obligations in the contract if all of the following criteria are met:

- (a) the entity regularly sells each distinct good or service (or each bundle of distinct goods or services) in the contract on a stand-alone basis;
- (b) the entity also regularly sells on a stand-alone basis a bundle (or bundles) of some of those distinct goods or services at a discount to the stand-alone selling prices of the goods or services in each bundle; and
- (c) the discount attributable to each bundle of goods or services described in (b) above is substantially the same as the discount in the contract and an analysis of the goods or services in each bundle provides observable evidence of the performance obligation (or performance obligations) to which the entire discount in the contract belongs.

Step 4:

Allocate the transaction price

Example

An entity enters into a contract with a customer to sell Products A, B and C in exchange for Rs. 10,000. The entity will satisfy the performance obligations for each of the products at different points in time. The entity regularly sells Product A separately and therefore the stand-alone selling price is directly observable. The stand-alone selling prices of Products B and C are not directly observable.

Because the stand-alone selling prices for Products B and C are not directly observable, the entity must estimate them. To estimate the stand-alone selling prices, the entity uses the adjusted market assessment approach for Product B and the expected cost plus a margin approach for Product C. In making those estimates, the entity maximises the use of observable inputs.

The entity estimates the stand-alone selling prices as follows:

Step 4:

Allocate the transaction price

Example(Cont.)

Product	Stand-alone Selling Price	Method
	Rs.	
Product A	5000	Directly observable
Product B	2500	Adjusted market assessment approach
Product C	7500	Expected cost plus a margin approach
Determine the transaction price allocated to each product. Total	15000	

Step 4:

Allocate the transaction price

Solution

The customer receives a discount for purchasing the bundle of goods because the sum of the stand-alone selling prices (Rs. 15,000) exceeds the promised consideration (Rs. 10,000). The entity considers that there is no observable evidence about the performance obligation to which the entire discount belongs. The discount is allocated proportionately across Products A, B and C.

The discount, and therefore the transaction price, is allocated as follows:

Product	Allocated transaction price (to nearest Rs.100)	
	Rs.	
Product A	3300	(Rs. 5,000 ÷ Rs. 15,000 × Rs. 10,000)
Product B	1700	(Rs. 2,500 ÷ Rs. 15,000 × Rs. 10,000)
Product C	5000	(Rs. 7,500 ÷ Rs. 15,000 × Rs. 10,000)
Total	10000	

Step 4:

Allocate the transaction price

Penalties

As per Ind AS 115.51AA, penalties shall be accounted for as per the substance of the contract.

Where the penalty is inherent in determination of transaction price, it shall form part of variable consideration.

For example, where an entity agrees to transfer control of a good or service in a contract with customer at the end of 30 days for Rs. 100,000 and if it exceeds 30 days, the entity is entitled to receive only Rs. 95,000, the reduction of Rs. 5,000 shall be regarded as variable consideration. In other cases, the transaction price shall be considered as fixed.

Step 4:

Allocate the transaction price

Changes in the transaction price

After contract inception, the transaction price can change for various reasons, including the resolution of uncertain events or other changes in circumstances that change the amount of consideration to which an entity expects to be entitled in exchange for the promised goods or services.

The following principles should be noted:

- An entity shall allocate to the performance obligations in the contract any subsequent changes in the transaction price on the same basis as at contract inception. Consequently, an entity shall not reallocate the transaction price to reflect changes in stand-alone selling prices after contract inception.
- Amounts allocated to a satisfied performance obligation shall be recognised as revenue, or as a reduction of revenue, in the period in which the transaction price changes.

When reallocating consideration because of a change in the transaction price, the entity continues to allocate the variable amount entirely to a performance obligation or to a distinct good or service that forms part of a single performance obligation if the criteria in Ind AS 115.85 (as discussed above) continue to be met.

If the change in transaction price is the result of a contract modification, the entity should follow the contract modification guidance.

Step 4:

Allocate the transaction price

Example

As On 1 April 20X0, a consultant enters into an arrangement to provide due diligence, valuation, and software implementation services to a customer for Rs. 2 crores. The consultant can earn Rs. 20 lakhs bonus if it completes the software implementation by 30 September 20X0 or Rs. 10 lakhs bonus if it completes the software implementation by 31 December 20X0.

The due diligence, valuation, and software implementation services are distinct and therefore are accounted for as separate performance obligations. The consultant allocates the transaction price, disregarding the potential bonus, on a relative stand-alone selling price basis as follows:

- Due diligence – Rs. 80 lakhs
- Valuation – Rs. 20 lakhs
- Software implementation – Rs. 1 crore

At contract inception, the consultant believes it will complete the software implementation by 30 January 20X1. After considering the factors in Ind AS 115, the consultant cannot conclude that a significant reversal in the cumulative amount of revenue recognized would not occur when the uncertainty is resolved since the consultant lacks experience in completing similar projects. As a result, the consultant does not include the amount of the early completion bonus in its estimated transaction price at contract inception.

Step 4:

Allocate the transaction price

Example(Cont.)

On 1 July 20X0, the consultant notes that the project has progressed better than expected and believes that implementation will be completed by 30 September 20X0 based on a revised forecast. As a result, the consultant updates its estimated transaction price to reflect a bonus of Rs. 20 lakhs.

After reviewing its progress as of 1 July 20X0, the consultant determines that it is 100 percent complete in satisfying its performance obligations for due diligence and valuation and 60 percent complete in satisfying its performance obligation for software implementation. Determine the transaction price.

Step 4:

Allocate the transaction price

Solution

On 1 July 20X0, the consultant allocates the bonus of Rs. 20 lakhs to the software implementation performance obligation, for total consideration of Rs. 1.2 crores allocated to that performance obligation, and adjusts the cumulative revenue to date for the software implementation services to Rs. 72 lakhs (60 percent of Rs. 1.2 crores).

Step 4:

Allocate the transaction price

Exceptions for variable consideration

- ▶ Variable consideration is required to be allocated to one or more (but not all) performance obligations if both of the following criteria are met:
 - ▶ The contingent payment relates specifically to the entity's efforts to satisfy that performance obligation
 - ▶ The amount allocated entirely to that performance obligation is consistent with the overall principle for allocating consideration
- ▶ This exception can be applied to a single performance obligation or a combination of performance obligations
- ▶ Subsequent changes in variable consideration should be allocated in a consistent manner

Step 4:

Example

Allocation of Transaction Price

- ▶ The price mentioned in the Purchase order is INR 50,00,000 for delivering a machine.
- ▶ This 50,00,000 should be allocated to the various performance obligations identified earlier on the basis of its stand-alone selling price.
- ▶ The stand-alone price at which the machinery is sold in the market is INR 48,00,000.
- ▶ The observable price for delivery service and packaging is not available.
- ▶ The cost related information is as follows -

Particular	Internal Cost per machine	Margin market would be willing to pay (%)	Stand-alone selling price
Packaging	83,333	20	1,00,000
Delivery service	4,34,783	15	5,00,000

Step 4:

Example

Allocation of Transaction Price

Performance Obligation	Stand – alone Selling Price	Allocation of Transaction Price
Sale of Product	48,00,000	44,44,444 (48,00,000/ 54,00,000 * 50,00,000)
Delivery Service	1,00,000	92,593 (1,00,000/ 54,00,000 * 50,00,000)
Packaging	5,00,000	4,62,963 (5,00,000/ 54,00,000 * 50,00,000)
Total	54,00,000	50,00,000

Step 5: Recognise revenue when (or as) each performance obligation is satisfied

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

- ▶ Revenue is recognised upon **satisfaction of a performance obligation** by transferring a good or service to a customer
 - ▶ A good or service is generally considered to be transferred when the customer obtains control
- ▶ Control transfers over time or at a point in time
- ▶ If none of the criteria for transfer over time are met (refer next slide to understand the criteria), control transfers at a point in time
- ▶ The following are indicators of when control is transferred:
 - ▶ The entity has a present right to payment for the good or service
 - ▶ The customer has legal title to the asset
 - ▶ The customer has physical possession
 - ▶ The customer has the significant risk and rewards of ownership of the asset
 - ▶ The entity has evidence of the customer's acceptance of the asset

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Control of goods and services is transferred over time if one of the following three criteria is met:

The entity's performance creates or enhances an asset that the customer controls as it is created or enhanced

The entity's performance does not create an asset with alternative use and the entity has a right to payment for performance completed to date

The customer is receiving and consuming the benefits of the entity's performance as the entity performs

If none of the criteria are met, control transfers at a point in time

- ▶ If control transfers over time, an entity selects a single **input or output method** to measure progress for a particular performance obligation
- ▶ Apply consistent method for all similar arrangements

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Example

Minitex Ltd. is a payroll processing company. Minitex Ltd. enters into a contract to provide monthly payroll processing services to ABC limited for one year. Determine how entity will recognise the revenue?

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Solution:

Payroll processing is a single performance obligation. On a monthly basis, as Microtek Ltd carries out the payroll processing

- The customer, ie, ABC Limited simultaneously receives and consumes the benefits of the entity's performance in processing each payroll transaction.
- Further, once the services have been performed for a particular month, in case of termination of the agreement before maturity and contract is transferred to another entity, then such new entity will not need to re-perform the services for expired months. Therefore, it satisfies the first criterion, ie, services completed on a monthly basis are consumed by the entity at the same time and hence, revenue shall be recognised over the period of time. For certain performance obligations, an entity may not be able to readily identify whether a customer simultaneously receives and consumes the benefits from the entity's performance as the entity performs. In such cases, a performance obligation is satisfied over time if an entity determines that another entity would not need to substantially re-perform the work that the entity has completed to date if that other entity were to fulfil the remaining performance obligation to the customer.

In making such determination, an entity shall make both of the following assumptions:

- (a) disregard potential contractual restrictions or practical limitations that otherwise would prevent the entity from transferring the remaining performance obligation to another entity; and
- (b) presume that another entity fulfilling the remainder of the performance obligation would not have the benefit of any work in progress.

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Example

T&L Limited ('T&L') is a logistics company that provides inland and sea transportation services. A customer – Horizon Limited ('Horizon') enters into a contract with T&L for transportation of its goods from India to Srilanka through sea. The voyage is expected to take 20 days Mumbai to Colombo. T&L is responsible for shipping the goods from Mumbai port to Colombo port. Whether T&L's performance obligation is met over period of time?

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Solution

T&L has a single performance to ship the goods from one port to another. The following factors are critical for assessing how services performed by T&L are consumed by the customer –

- As the voyage is performed, the service undertaken by T&L is progressing, such that no other entity will need to re-perform the service till so far as the voyage has been performed, if T&L was to deliver only part-way.
- The customer is directly benefitting from the performance of the voyage as & when it progresses. Therefore, such performance obligation is said to be met over a period of time.

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Example

AFS Ltd. is a risk advisory firm and enters into a contract with a company – WBC Ltd to provide audit services that results in AFS issuing an audit opinion to the Company. The professional opinion relates to facts and circumstances that are specific to the company. If the Company was to terminate the consulting contract for reasons other than the entity's failure to perform as promised, the contract requires the Company to compensate the risk advisory firm for its costs incurred plus a 15 per cent margin. The 15 per cent margin approximates the profit margin that the entity earns from similar contracts. Whether risk advisory firm's performance obligation is met over period of time?

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Solution

AFS has a single performance to provide an opinion on the professional audit services proposed to be provided under the contract with the customer. Evaluating the criterion for recognising revenue over a period of time or at a point in time, Ind AS 115 requires one of the following criterion to be met –

- Criterion (a) – whether the customer simultaneously receives and consumes the benefits from services provided by AFS: Company shall benefit only when the audit opinion is provided upon completion. And in case the contract was to be terminated, any other firm engaged to perform similar services will have to substantially re-perform. Hence, this criterion is not met.
- Criterion (b) – An asset created that customer controls: This is service contract and no asset created, over which customer acquires control.
- Criterion (c) – no alternate use to entity and right to seek payment:
 - ❖ The services provided by AFS are specific to the company – WBC and do not have any alternate use to AFS
 - ❖ Further, AFS has a right to enforce payment if contract was early terminated, for reasons other than AFS's failure to perform. And the profit margin approximates what entity otherwise earns.

Therefore, criterion (c) is met and such performance obligation is said to be met over a period of time.

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Example

Space Ltd. enters into an arrangement with a government agency for construction of a space satellite. Although Space Ltd is in this business for building such satellites for various customers across the world, however the specifications for each satellite may vary based on technology that is incorporated in the satellite. In the event of termination, Company has right to enforce payment for work completed to date.

Evaluate if contract will qualify for satisfaction of performance obligation over a period of time.

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Solution

While evaluating the pattern of transfer of control to the customer, the Company shall evaluate conditions laid in para 35 of Ind AS 115 as follows:

- Criterion (a) – whether the customer simultaneously receives and consumes the benefits: Customer can benefit only when the satellite is fully constructed and no benefits are consumed as its constructed. Hence, this criterion is not met.
 - Criterion (b) – An asset created that customer controls: Per provided facts, the customer does not acquire control of the asset as its created.
 - Criterion (c) – no alternate use to entity and right to seek payment:
 - ❖ The asset is being specifically created for the customer. The asset is customised to customer's requirements, such that any diversion for a different customer will require significant work. Therefore, the asset has practical limitation in being put to alternate use.
 - ❖ Further, Space Ltd.has a right to enforce payment if contract was early terminated, for reasons other than Space Ltd.'s failure to perform.
- Therefore, criterion (c) is met and such performance obligation is said to be met over a period of time.

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Example

ABC enters into a contract with a customer to build an item of equipment. The customer pays 10% advance and then 80% in instalments of 10% each over the period of construction with balance 10% payable at the end of construction period. The payments are non-refundable unless the company fails to perform as per the contract. Further, if the customer terminates the contract, then entity is entitled to retain payments made. The company will have no further right to compensation from the customer.

Evaluate if contract will qualify for satisfaction of performance obligation over a period of time.

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Example

The Company shall evaluate conditions laid in para 35 of Ind AS 115 as follows:

- Criterion (a) – whether the customer simultaneously receives and consumes the benefits: Customer can benefit only when the asset is fully constructed and no benefits are consumed as its constructed. Hence, this criterion is not met.
- Criterion (b) – An asset created that customer controls: Per provided facts, the customer does not acquire control of the asset as its created.
- Criterion (c) – no alternate use to entity and right to seek payment:
 - ❖ The customer has specific right over the asset and company does not have right to divert it for any alternate use. In other words, there is contractual restriction to use the asset for any alternate purpose.
 - ❖ In the event of early termination, Company has a right to retain any payments made by the customer. However, such payments need not necessarily compensate the selling price of the partially constructed asset, if the customer was to stop making payments.

Therefore, Company does not have a legally enforceable right to payment for work completed to date and the criterion under para 35 is not. Thus, revenue cannot be recognised over a period of time.

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Measure progress

Methods that can be used to measure an entity's progress towards complete satisfaction of a performance obligation satisfied over time

Output method

- ▶ “Output methods” recognize revenue on the basis of direct measurements of the value to the customer of the goods or services transferred to date relative to the remaining goods or services promised under the contract.
- ▶ Output methods include methods such as surveys of performance completed to date, appraisals of results achieved, milestones reached, time elapsed, and units produced or units delivered.

Input method

- ▶ “Input methods” recognize revenue on the basis of the entity's efforts or inputs to the satisfaction of a performance obligation (for example, resources consumed, labour hours expended, costs incurred, time elapsed, or machine hours used) relative to the total expected inputs to the satisfaction of that performance obligation

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Example

An entity, an owner and manager of health clubs, enters into a contract with a customer for one year of access to any of its health clubs. The customer has unlimited use of the health clubs and promises to pay CU100 per month. The entity's promise to the customer is to provide a service of making the health clubs available for the customer to use as and when the customer wishes.

Evaluate if contract will qualify for satisfaction of performance obligation over a period of time. If yes, how should an entity measure its progress of service provided?

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Solution

The entity shall determine if revenue should be recognised over a period of time by evaluating the conditions laid in para 35 of Ind AS 115.

- Applying the first criterion of para 35 to establish if the customer simultaneously receives and consumes the benefits, as the entity provides service – The health club provides access to services uniformly through the year. The extent to which the customer uses the health clubs does not affect the amount of the remaining goods and services to which the customer is entitled. The customer therefore simultaneously receives and consumes the benefits of the entity's performance as it performs by making the health clubs available.
- Consequently, the entity's performance obligation is satisfied over time
- Once the pattern of satisfying performance obligation is defined, the Company then determines how progress should be measured. The services are uniformly provided to the customer through the year. Therefore, the best measure of progress is to recognise revenue on a straight line basis over the year.

Step 5:

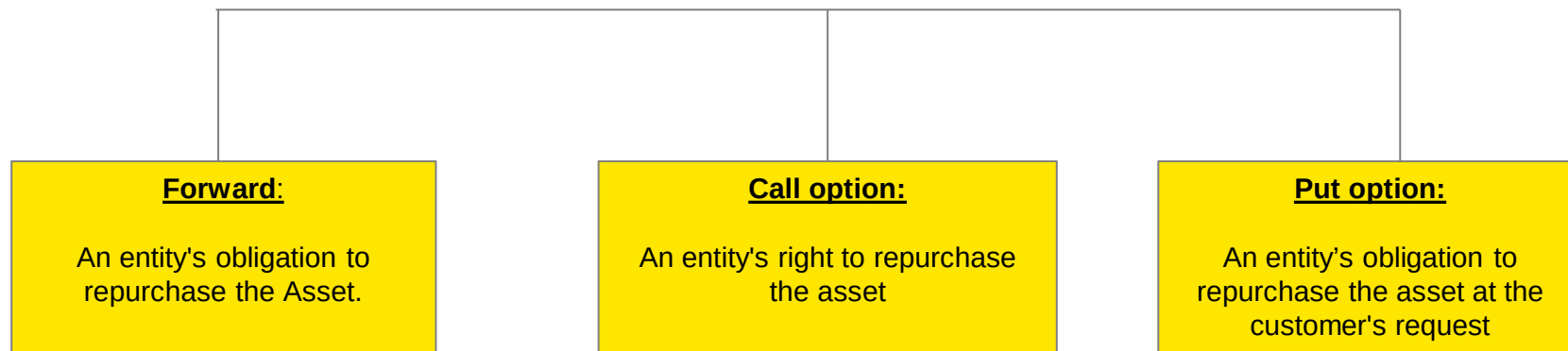
Recognise revenue when (or as) performance obligations are satisfied

Repurchase Agreement

When a company determines the timing of transfer of control, it is important to take into consideration any repurchase agreements that may have been executed by the Company.

A repurchase agreement is a contract in which an entity sells an asset and also promises or as the option (either in the same contract or in another contract) to repurchase the asset. The repurchased asset may be the asset that was originally sold to the customer, an asset that is substantially the same as that asset, or another asset of which the asset that was originally sold is a component.

Repurchase agreements generally come in three forms



Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Example

An entity enters into a contract with a customer for the sale of a tangible asset on 1 January 20X1 for Rs. 1 million. The contract includes a call option that gives the entity the right to repurchase the asset for Rs. 1.1 million on or before December 31, 20X1.

How would the entity account for this transaction?

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Solution

In the above case, where the entity has a right to call back the goods upto a certain date –

- The customer cannot be said to have acquired control, owing to the repurchase right with the seller entity
- Since the original selling price (Rs. 1 million) is lower than the repurchase price (Rs. 1.1 million), this is construed to be a financing arrangement and accounted as follows:

(a) Amount received shall be recognized as 'liability'

(b) Difference between sale price and repurchase price to be recognised as 'finance cost' and recognised over the repurchase term.

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Example

An entity enters into a contract with a customer for the sale of a tangible asset on 1 January 20X1 for Rs. 1,000,000. The contract includes a put option that gives the customer the right to sell the asset for Rs. 900,000 on or before December 31, 20X1. The market price for such goods is expected to be Rs. 750,000

How would the entity account for this transaction?

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Solution

In the above case, where the entity has an obligation to buy back the goods upto a certain date –

- The entity shall evaluate if the customer has a significant economic incentive to return the goods. Since the repurchase price is significantly higher than market price, therefore, customer has a significant economic incentive to return the goods. There are no other factors which entity may affect this assessment.
- Therefore, company determines that 'control' of goods is not transferred to the customer till 31 December 20X1, ie, till the put option expires.
- Against payment of Rs. 1,000,000; the customer only has a right to use the asset and put it back to the entity for Rs. 900,000. Therefore, this will be accounted as a lease transaction in which difference between original selling price (ie, Rs. 1,000,000) and repurchase price (ie, Rs. 900,000) shall be recognized as lease income over the period of lease.
- At the end of repurchase term, ie, 31 December 20X1, if the customer does not exercise such right, then the control of goods would be passed to the customer at that time and revenue shall be recognized for sale of goods for repurchase price (ie, Rs. 900,000).

Step 5:

Recognise revenue when (or as) performance obligations are satisfied – Bill and hold criteria

- ▶ Criteria for qualifying for revenue recognition on bill-and-hold arrangements are similar to current IFRS
 - ▶ The reason must be substantive
 - ▶ The product must be identified separately
 - ▶ The product currently must be ready for physical transfer
 - ▶ The entity cannot have the ability to use the product or to direct it to another customer
- ▶ Entities that record revenue on bill-and-hold arrangements should monitor developments in this area

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Example

An entity enters into a contract with a customer on 1 April 20X1 for the sale of a machine and spare parts. The manufacturing lead time for the machine and spare parts is two years. Upon completion of manufacturing, the entity demonstrates that the machine and spare parts meet the agreed-upon specifications in the contract. The promises to transfer the machine and spare parts are distinct and result in two performance obligations that each will be satisfied at a point in time. On 31 March 20X3, the customer pays for the machine and spare parts, but only takes physical possession of the machine. Although the customer inspects and accepts the spare parts, the customer requests that the spare parts be stored at the entity's warehouse because of its close proximity to the customer's factory. The customer has legal title to the spare parts and the parts can be identified as belonging to the customer. Furthermore, the entity stores the spare parts in a separate section of its warehouse and the parts are ready for immediate shipment at the customer's request. The entity expects to hold the spare parts for two to four years and the entity does not have the ability to use the spare parts or direct them to another customer.

How will the Company recognise revenue for sale of machine and spare parts? Is there any other performance obligation attached to this sale of goods?

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Solution

In the facts provided above, the entity has made sale of two goods – machine and spare parts, whose control is transferred at a point in time. Additionally, company agrees to hold the spare parts for the customer for a period of 2-4 years, which is a separate performance obligation. Therefore, total transaction price shall be divided amongst 3 performance obligations –

- (i) Sale of machinery
- (ii) Sale of spare parts
- (iii) Custodial services for storing spare parts.

Recognition of revenue for each of the three performance obligations shall occur as follows:

- Sale of machinery: Machine has been sold to the customer and physical possession as well as legal title passed to the customer on 31 March 20X3. Accordingly, revenue for sale of machinery shall be recognised on 31 March 20X3.

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Solution(Cont.)

- Sale of spare parts: The customer has made payment for the spare parts and legal title has been passed to specifically identified goods, but such spares continue to be physically held by the entity. In this regard, the company shall evaluate if revenue can be recognized on bill-n-hold basis if all below criteria are met:

(a) the reason for the bill-and-hold arrangement must be substantive (for example, the customer has requested the arrangement);	The customer has specifically requested for entity to store goods in their warehouse, owing to close proximity to customer's factory.
(b) the product must be identified separately as belonging to the customer;	The spare parts have been specifically identified and inspected by the customer.
(c) the product currently must be ready for physical transfer to the customer; and	The spares are identified and segregated, therefore, ready for delivery.
(d) the entity cannot have the ability to use the product or to direct it to another customer	Spares have been segregated and cannot be redirected to any other customer.

Step 5:

Recognise revenue when (or as) performance obligations are satisfied

Solution(Cont.)

Therefore, all conditions of bill-and-hold are met and hence, company can recognize revenue for sale of spare parts on 31 March 20X3.

- Custodial services: Such services shall be given for a period of 2 to 4 years from 31 March 20X3. Where services are given uniformly and customer receives & consumes benefits simultaneously, revenue for such service shall be recognized on a straight line basis over a period of time.

OTHER TOPICS

Contract costs

- ▶ **Incremental costs of obtaining a contract** are capitalised if they are expected to be recovered
 - ▶ Incremental costs are costs that would not have been incurred if the contract had not been obtained
 - ▶ Practical expedient to allow immediate expense recognition if the amortisation period of the asset would be one year or less
- ▶ **Costs of fulfilling a contract** (that are not addressed by another standard) are capitalised if they:
 - ▶ Relate directly to a contract or to a specifically anticipated contract
 - ▶ Generate or enhance resources that will be used to satisfy performance obligations in the future
 - ▶ Are expected to be recovered
- ▶ Assets are amortised over the period the goods or services are transferred and are subject to impairment review



Licenses



A licence establishes a customer's rights to intellectual property (IP) of the entity



Entity must first determine whether the licence is a distinct performance obligation in the arrangement

For a distinct licence, assess the nature of the promise



For a licence providing a **right to access the IP**, revenue is recognised over time if specific criteria are met



For a licence providing a **right to use the IP** as it exists when granted, revenue is recognised at a point in time

Sales- or usage-based royalties on licences of IP

Royalties cannot be recognised as revenue until the later of when the sale/usage occurs or the performance obligation is satisfied

Licenses

A distinct licence could represent either:



Access to the IP (over time)



The contract requires, or the customer reasonably expects, that the entity will undertake activities that significantly affect the licensed IP



The rights granted by the licence directly expose the customer to any effects of the entity's activities



The entity's activities do not result in the transfer of a good or service to the customer as the activities occur



All criteria must be met



Right to use the IP (at a point in time)



If all three criteria for access (over time) are not met, the nature of the entity's promise is to provide a right to use the IP as the IP exists at the point in time at which the licence is granted to the customer.



Effectively, this means the customer is able to direct the use of and obtain all remaining benefits from the licensed IP when granted (i.e., the IP is static)

Presentation and disclosure

Presentation

- ▶ A contract liability is an entity's obligation to transfer goods or services to a customer for which the entity has received consideration (or an amount of consideration is due) from the customer.
- ▶ A contract asset is an entity's right to consideration in exchange for goods or services that the entity has transferred to a customer
- ▶ A receivable is an entity's right to consideration that is unconditional. A right to consideration is unconditional if only the passage of time is required before payment of that consideration is due.
- ▶ These assets or liabilities are presented in the balance sheet depending on the relationship between the entity's performance and the customer's payment.
- ▶ Contract assets and receivables are subject to impairment review in accordance with Ind AS 109.
- ▶ An entity shall present separately the amount of excise duty included in the revenue recognised in the statement of profit and loss.



Disclosures

Contracts with customers for annual periods

Impact	Disclosure Category	Key Disclosures
High	Contract balance	▶ Opening / closing balances of receivables, contract assets / liabilities ▶ Revenue recognized in reporting period that was included in the contract liability ▶ Revenue recognized in reporting period from performance obligations satisfied in previous period ▶ Explanation of the significant changes in the contract asset and contract liability balances ▶ Relation between timing of satisfaction of its performance obligations and timing of payment.
	Costs to obtain or fulfill a contract	▶ Judgments made in determining the amount of the costs incurred to obtain or fulfill a contract with a customer and the method it uses to determine the amortization for each reporting period.
Medium	Disaggregation of revenue	▶ Disaggregation of revenue into categories that depict how the nature, amount, timing, and uncertainty of revenue and cash flows are affected by economic factors.
	Performance obligation	▶ Disclosure of significant payment terms and the nature of the goods or services promised to transfer.
	Significant Judgment	▶ Significant judgments made that affect the determination of the amount and timing of revenue ▶ Method use to recognise revenue, in case of performance obligation satisfied over a period of time. ▶ Significant judgments made in evaluating when the customer obtains control of goods or services. ▶ Disclosure of methods, inputs and assumptions used.
Low	Contracts with customer	▶ Impairment losses on contract assets or receivables shall be disclosed separately from impairment losses from other contracts
	Performance obligation	▶ Disclosure about performance obligations in contracts with customers ▶ Disclose the aggregate amount of the transaction price allocated to remaining performance obligations ▶ Adoption of practical expedient and its disclosure
	Practical Expedient	▶ Adoption of practical expedient as per Ind AS 115 and its disclosure

SERVICE CONCESSION ARRANGEMENTS

About Arrangement

- Service Concession Arrangement involves a private sector entity (an operator) constructing the infrastructure used to provide the public service or upgrading it (for example, by increasing its capacity) and operating and maintaining that infrastructure for a specified period of time. The operator is paid for its services over the period of the arrangement. The arrangement is governed by a contract that sets out performance standards, mechanisms for adjusting prices, and arrangements for arbitrating disputes.
- Such an arrangement is often described as a 'build-operate-transfer', a 'rehabilitate-operate-transfer' or a 'public-to-private' service concession arrangement.

SERVICE CONCESSION ARRANGEMENTS

Example

Infrastructure for public services—such as roads, bridges, tunnels, prisons, hospitals, airports, water distribution facilities, energy supply and telecommunication networks —has traditionally been constructed, operated and maintained by the public sector and financed through public budget appropriation.

SERVICE CONCESSION ARRANGEMENTS

Accounting Principles

- Treatment of the operator's rights over the infrastructure
- Recognition and measurement
- Consideration given by the grantor to the operator
- Contractual obligations to restore the infrastructure to a specified level of serviceability.
- Borrowing costs incurred by the operator
- Financial asset
- Intangible asset
- Items provided to the operator by the grantor

SERVICE CONCESSION ARRANGEMENTS

Treatment of the operator's rights over the infrastructure

- Infrastructure shall not be recognised as property, plant and equipment of the operator because the contractual service arrangement does not convey the right to control the use of the public service infrastructure to the operator.
- The operator has access to operate the infrastructure to provide the public service on behalf of the grantor in accordance with the terms specified in the contract.

SERVICE CONCESSION ARRANGEMENTS

Recognition and measurement

- Since the operator acts as a service provider, he shall recognise and measure revenue in accordance with Ind AS 115 for the services it performs. The operator constructs or upgrades infrastructure (construction or upgrade services) used to provide a public service and operates and maintains that infrastructure (operation services) for a specified period of time.
- If the operator performs more than one service (ie construction or upgrade services and operation services) under a single contract or arrangement, consideration received or receivable shall be allocated by reference to the relative fair values of the services delivered, when the amounts are separately identifiable.
- The nature of the consideration i.e. whether financial asset or intangible asset determines its subsequent accounting treatment.
- The operator shall account for revenue and costs relating to construction or upgrade services.
- The operator shall account for revenue and costs relating to operation services in accordance with Ind AS 115.

SERVICE CONCESSION ARRANGEMENTS

Consideration given by the grantor to the operator

- If the operator provides construction or upgrade services the consideration received or receivable by the operator shall be recognized at its fair value. The consideration may be rights to:
 - (a) a financial asset, or
 - (b) an intangible asset.
- The operator shall recognise a financial asset to the extent that
 - it has an unconditional contractual right to receive cash or another financial asset from or at the direction of the grantor for the construction services; the grantor has little, if any, discretion to avoid payment, usually because the agreement is enforceable by law.
 - it has an unconditional right to receive cash if the grantor contractually guarantees to pay the operator (a) specified or determinable amounts or (b) the shortfall, if any, between amounts received from users of the public service and specified or determinable amounts, even if payment is contingent on the operator ensuring that the infrastructure meets specified quality or efficiency requirements.
- The operator shall recognise an intangible asset to the extent that it receives a right (a licence) to charge users of the public service. A right to charge users of the public service is not an unconditional right to receive cash because the amounts are contingent on the extent that the public uses the service.
- If the operator is paid for the construction services partly by a financial asset and partly by an intangible asset it is necessary to account separately for each component of the operator's consideration. The consideration received or receivable for both components shall be recognised initially at the fair value of the consideration received or receivable.

SERVICE CONCESSION ARRANGEMENTS

Contractual obligations to restore the infrastructure to a specified level of serviceability.

The operator may have contractual obligations it must fulfil as a condition of its licence, like to maintain or restore infrastructure, except for any upgrade element, which shall be recognised and measured in accordance with Ind AS 37, ie at the best estimate of the expenditure that would be required to settle the present obligation at the end of the reporting period.

SERVICE CONCESSION ARRANGEMENTS

Borrowing costs incurred by the operator

- Borrowing costs attributable to the arrangement shall be recognised as an expense in the period in which they are incurred unless the operator has a contractual right to receive an intangible asset (a right to charge users of the public service).
- If the operator does not have a contractual right to receive an intangible asset, borrowing costs attributable to the arrangement shall be capitalised during the construction phase of the arrangement.

SERVICE CONCESSION ARRANGEMENTS

Financial asset

- For recognition of financial asset, Ind AS 32, Ind AS 107 and Ind AS 109 shall be applied. The amount due from or at the direction of the grantor is accounted at:
 - (a) amortised cost;
 - (b) fair value through other comprehensive income; or
 - (c) fair value through profit or loss.
- If the amount due from the grantor is measured at amortised cost or fair value through other comprehensive income, Ind AS 109 requires interest calculated using the effective interest method to be recognised in profit or loss.

SERVICE CONCESSION ARRANGEMENTS

Intangible asset

For recognition and measurement of intangible asset, one has to apply Ind AS 38 for guidance on measuring intangible assets acquired in exchange for a non-monetary asset or assets or a combination of monetary and non-monetary assets.

Items provided to the operator by the grantor

- Infrastructure items to which the operator is given access by the grantor for the purposes of the service arrangement are not recognised as property, plant and equipment of the operator.
- The grantor may also provide other items to the operator that the operator can keep or deal with as it wishes. If such assets form part of the consideration payable by the grantor for the services, they are not government grants as defined in Ind AS 20. They are recognised as assets of the operator, measured at fair value on initial recognition.
- The operator shall recognise a liability in respect of unfulfilled obligations it has assumed in exchange for the assets.

SERVICE CONCESSION ARRANGEMENTS

Service Concession Arrangements: Disclosures

- All aspects of a service concession arrangement shall be considered in determining the appropriate disclosures in the notes. An operator and a grantor shall disclose the following in each period:

- (a) a description of the arrangement;
- (b) significant terms of the arrangement that may affect the amount, timing and certainty of future cash flows (eg the period of the concession, re-pricing dates and the basis upon which re-pricing or re-negotiation is determined);
- (c) the nature and extent (eg quantity, time period or amount as appropriate) of:
 - (i) rights to use specified assets;
 - (ii) obligations to provide or rights to expect provision of services;
 - (iii) obligations to acquire or build items of property, plant and equipment;
 - (iv) obligations to deliver or rights to receive specified assets at the end of the concession period;
 - (v) renewal and termination options; and
 - (vi) other rights and obligations (eg major overhauls);
- (d) changes in the arrangement occurring during the period; and
- (e) how the service arrangement has been classified.

- An operator shall disclose the amount of revenue and profits or losses recognized in the period on exchanging construction services for a financial asset or an intangible asset.

- The disclosures required in accordance with paragraph 6 of this Appendix shall be provided individually for each service concession arrangement or in aggregate for each class of service concession arrangements. A class is a grouping of service concession arrangements involving services of a similar nature (eg toll collections, telecommunications and water treatment services).

GAAP Differences – Ind AS Vs AS

Key GAAP differences

Particulars	Ind AS 115	AS 7 and AS 9
Framework of Revenue Recognition	Ind AS 115 gives a framework of revenue recognition within a standard. It specifies the core principle for revenue recognition which requires the 'revenue to depict the transfer of promised 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'.	AS 7 and AS 9 do not provide any such overarching principle to fall upon in case of doubt.
Comprehensive Guidance on Recognition and Measurement of Multiple Elements within a Contract with Customer	Ind AS 115 gives comprehensive guidance on how to recognise and measure multiple elements within a contract with customer.	AS 7 and AS 9 do not provide comprehensive guidance on this aspect.

Key GAAP differences

Particulars	Ind AS 115	AS 7 and AS 9
Coverage	Ind AS 115 comprehensively deals with all types of performance obligation contract with customer. However, it does not deal with revenue from 'interest' and 'dividend' which are covered in financial instruments standard.	AS 7 covers only revenue from construction contracts which is measured at consideration received / receivable. AS 9 deals only with recognition of revenue from sale of goods, rendering of services, interest, royalties and dividends.
Measurement of Revenue	As per Ind AS 115, revenue is measured at transaction price, i.e., the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties.	- As per AS 9, Revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities. Revenue is measured by the charges made to customers or clients for goods supplied and services rendered to them and by the charges and - rewards arising from the use of resources by them. As per AS 7, revenue from construction contracts is measured at consideration received / receivable and to be recognised as revenue as construction progresses, if certain conditions are met.
Recognition of Revenue	As per Ind AS 115, revenue is recognised when the control is transferred to the customer.	As per AS 9, revenue is recognised when significant risks and rewards of ownership is transferred to the buyer. As per AS 7, revenue is recognised when the outcome of a construction contract can be estimated reliably, contract revenue should be recognised by reference to the stage of completion of the contract activity at the reporting date.

Key GAAP differences

Particulars	Ind AS 115	AS 7 and AS 9
• Capitalisation of Costs	• Ind AS 115 provides guidance on recognition of costs to obtain and fulfill a contract, as asset	• AS 7 and AS 9 do not deal with such capitalisation of costs.
• Guidance on Service Concession Arrangements	• Ind AS 115 gives guidance on service concession arrangements and disclosures thereof	• AS does not provide such guidance.
• Disclosure Requirements	• Ind AS 115 contains detailed disclosure requirements.	• Less disclosure requirements are prescribed in AS

Thank You