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Accounting for revenue is changing

What's the impact on telecommunication companies?

The new revenue standard – effective from 1 January 2018 – is likely to affect the way you account for revenue. But it is more than just an accounting change.

It could impact:

- timing of revenue recognition – e.g.:
  - greater up-front revenue on subsidised handsets
  - disconnect between the reported revenue and the amount billed
  - decrease in the average revenue per user for ongoing services
  - deferral of revenue on up-front fee related to future services
- deferral and amortisation of contract costs and commissions
- arrangements with dealers
- systems and processes, including data collection
- revenue-based metrics
- disclosures in annual and interim reports

It's time to engage, particularly as there are also new standards on leases and financial instruments.

If you have:

- subsidised handsets
- multiple-user plans
- early upgrade rights
- non-refundable fees for set-up services
- customer retention discounts
- contracts paid over more than a year
- indirect channel sales
- commissions and other contract costs

…it's time to start looking at your contracts and assessing how the new revenue requirements will affect your business.

Engage with your stakeholders to build expectations of how your KPIs or business practices may change.

Determining the impact

Subsidised handsets

Potential impact

- Companies need to allocate a contract's transaction price to each performance obligation based on their relative stand-alone selling price. As a result, companies will recognise a greater amount of revenue on subsidised handsets up-front.
- This will result in a disconnect between the reported revenue and the amount billed. This will decrease the average revenue per user for ongoing services.

Actions to consider

- Develop new processes and adjust systems to capture, estimate and monitor stand-alone selling prices.
- Assess whether billing management systems are capable of supporting the allocation methodology and generation of journals to allocate revenue.
- Identify commercial opportunities by considering whether any contract terms or business practices should be modified.

Portfolio accounting

Potential impact

- Companies can choose to apply the standard to a portfolio of contracts or performance obligations with similar characteristics if the outcome isn't materially different than contract-by-contract accounting.
- Effort and outlay may be needed to:
  - evaluate which items constitute a portfolio considering, for example, the impact of different offerings, periods of time, geographic locations and contract modifications; and
  - assess, on an ongoing basis, whether the portfolio approach gives a materially different result.

Actions to consider

- Exercise judgement in determining when the portfolio approach may be appropriate, including considering whether any customer-specific agreements would be eligible.
- Develop the record-keeping to track and compare contract terms over large numbers of individual contracts.
- Develop the process and controls to account for and monitor portfolios over time through contract events such as repricing, changes in scope or duration.
- Ensure that portfolio record-keeping is fit for the purpose of regulatory and tax reporting.

Multiple-user plans

Potential impact

- Companies need to determine the appropriate unit of account for multiple-user plans under which individuals can share services – e.g. data or minutes – among themselves at discounted prices.
- The key question: is there one contract or multiple individual contracts? If accounting is on a combined basis, companies need to consider the implications of contract modifications to an individual's specific plan.
- Companies may also need to estimate the stand-alone selling price of each user's plan to allocate the transaction price.

Actions to consider

- Review the contractual terms and business practices related to multiple-user plans and determine the appropriate unit of account – either as individual contracts or as a combined contract.
- Assess how to account for modifications to the goods or services in an individual's plan within a multiple-user contract.
- Develop valuation models or processes to estimate stand-alone selling prices.

Early upgrade rights

Potential impact

- Companies that offer early upgrade rights – e.g. for handsets – need to determine the appropriate accounting, including whether a material right has been granted to the customer, if the right affects the transaction price, if modification accounting applies or if waived amounts are an incentive to enter into a new contract.
- A material right is an option to acquire additional goods or services at a price that does not reflect the good's or service's stand-alone selling price, and is considered a separate performance obligation.

Actions to consider

- Review all arrangements and business practices for early upgrade rights and exercise judgement in determining the appropriate accounting.
- Develop new processes and adjust systems to track and monitor separate components in a contract, including upgrade rights.

Non-refundable fees for set-up services

Potential impact

- Companies will need to evaluate whether up-front set-up and installation services are separate performance obligations. In many cases, though a non-refundable fee relates to a required activity – e.g. switching on access to the network – the activity does not result in the transfer of a promised good or service. In such cases, the nonrefundable fee is recognised as revenue when the future services are provided.
- The revenue recognition period for the non-refundable fee may not be consistent with the initial contractual period if the company grants the customer the option to renew the contract without repaying the fee.

Actions to consider

- Review all arrangements with non-refundable up-front fees and exercise judgement in assessing when to bundle or unbundle them.
- For contracts with renewal options, exercise judgement in evaluating whether a material right has been granted to the customer or whether the future optionality is a marketing promotion.
- Assess the revenue recognition period for non-refundable up-front fees, especially in relation to renewal options and early termination practices.

Customer retention discounts

Potential impact

- Even if customer retention discounts aren't explicit in the contract, customary business practice could mean that fixed consideration is, in substance, variable. Alternatively, such discounts could be viewed as contract modifications.
- Companies will need to assess whether the discount is variable consideration or a contract modification. This will require judgement and may impact the timing of revenue recognition.
- Companies will need to assess whether promotional offers to current customers are contract modifications or marketing transactions.

Actions to consider

- Assess whether processes and systems are capable of tracking and monitoring all discounts, concessions and promotional offers granted to customers.
- Review customer retention and pricing policies.
- Review current business practices in identifying any implicit promised price concession.
- Exercise judgement to assess whether these discounts are variable consideration and, if so, determine how to apply the constraint in estimating whether a significant revenue reversal is expected.

Contracts paid over more than a year

Potential impact

- If a customer can pay for purchased equipment over a period exceeding one year along with network services, then judgement is required to determine if the contract includes a significant financing component.
- If the contract includes a significant financing component, then the company needs to adjust the transaction price to reflect the time value of money.

Actions to consider

- Review all contracts that span more than one year and exercise judgement in assessing whether a significant financing component exists.
- Determine processes for estimating discount rates and ensure that systems can handle the resulting complex calculations.

Indirect channel sales

Potential impact

- Some companies may sell handsets and network services through dealers.
- The timing and presentation of handset sales could be affected as well as the accounting for reimbursements to the dealer for equipment subsidies when customers sign up for future services.
- The key question is whether the dealer is acting as an agent or a principal in the sale of the handset.

Actions to consider

- Review the contractual terms in place with dealers and the practical operation of such arrangements.
- Exercise judgement in determining how to account for reimbursements – e.g. commissions and handset subsidies – and whether to recognise revenue on a gross or a net basis.

Commissions and other contract costs

Potential impact

- Companies are required to capitalise incremental contract acquisition costs – e.g. sales commissions – and other contract fulfilment costs – e.g. installation costs – if they expect to recover these costs. However, a company may choose to expense contract acquisition costs if the amortisation period of the resulting asset is one year or less.
- Companies will need to exercise judgement in distinguishing between incremental costs incurred as a result of obtaining a contract and those that relate to satisfying a performance obligation.

Actions to consider

- Assess any required changes to existing systems to capture incremental costs and processes to determine and monitor the amortisation periods.
- Analyse any impacts on key performance indicators such as subscriber acquisition costs and subscriber retention costs.
- Exercise judgement in determining appropriate amortisation periods and in assessing whether the practical expedient is available when there is a possibility of contract renewals.

Transition options

Potential impact

- IFRS 15 may be adopted retrospectively, by restating comparatives and adjusting retained earnings at the beginning of the earliest comparative period.
- Alternatively, IFRS 15 may be adopted as of the application date, by adjusting retained earnings at the beginning of the first reporting year (the cumulative effect approach).

Actions to consider

- Quantify and evaluate the effects of the different transition options, including the available practical expedients under the retrospective approach.
- Perform a historical analysis of contracts. Consider whether existing systems provide the data required to produce comparative information if the new standard is applied retrospectively.

How KPMG can help

Assess the impacts

Design the right solution

Implement a future state

A robust assessment phase is critical to laying the framework for a successful project, and it is important to start the assessment early to provide flexibility during the implementation phase. An assessment phase typically includes the following activities:

Activities	Actions	Deliverables
Accounting diagnostic	• Identify potential gaps to accounting policy and disclosures by reviewing current accounting policy and sample of contracts • Leverage your existing documents and knowledge	Gap matrix, heat map and contract review summaries
Process and information gap analysis	• Identify new information and process requirements • Trace requirements to existing sources or identify gaps	Business requirements document, process and information gap analysis report
Technology and broader impact evaluation	• Identify potential impact on IT, tax, controls, operations, financial planning and analysis, investor relations etc. • Identify gaps and linkages across the organisation	Final gap matrix and heat map, implementation roadmap
Transition option assessment	• Determine how each option may impact financials and business • Assess readiness to elect the retrospective or cumulative effect option	Transition option assessment report

KPMG's Telecommunications practice

KPMG's Telecommunications practice is dedicated to supporting telecommunications carriers globally in understanding industry trends and business issues.

Member firms offer customised, industry-tailored services that can lead to value-added assistance for your most pressing business requirements.

At KPMG, our extensive network of professionals experienced in telecommunication practice combines global perspective with in-depth industry knowledge to help companies adjust to today's rapidly changing market.

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