

6. Revenue



Summary

This chapter covers:

- Ind AS 115, *Revenue from Contracts with Customers*



Ind AS 115 lays down the principles to be followed for recognition, measurement, and disclosures in respect of revenue from contract with customers.



Key principles

Overview of the five-step model

- **Step 1: Identify the contract with customer**

A contract is an agreement between two or more parties that creates enforceable rights and obligations. It may be written, oral or implied by customary business practices and meets all of the following criteria:

- It is legally enforceable
- It is approved and all the parties are committed to their obligations
- Rights to goods or services and payment terms can be identified
- Collection of consideration is considered probable

- It has 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.





• Step 2: Identify the performance obligations in the contract

- At contract inception, entities are required to identify as a performance obligation an implicit or an explicit promise to transfer to the customer a distinct good or service (or bundle of goods or services)
- A good or service that is promised to a customer is distinct if both the following criteria are met:
 - * *The good or service is capable of being distinct:* Customers could benefit from the good or service on its own or with other readily available resources. Various factors may provide such evidence, such as when the good or service can be used, consumed, sold for an amount that is greater than scrap value or held in a way that generates economic benefits.
 - * *The promise to transfer the good or service is distinct within the context of the contract:* The promise to transfer the good or service is separately identifiable from other promises in the contract.

• Step 3: Determine the transaction price

Determination of transaction price is done by considering all amounts to which an entity expects to be entitled in exchange for transferring promised goods or services excluding amounts collected on behalf of third parties (for example, some sales taxes). Additionally, the consideration may include fixed amounts, variable amounts, or both.

• Step 4: Allocating the transaction price to performance obligation

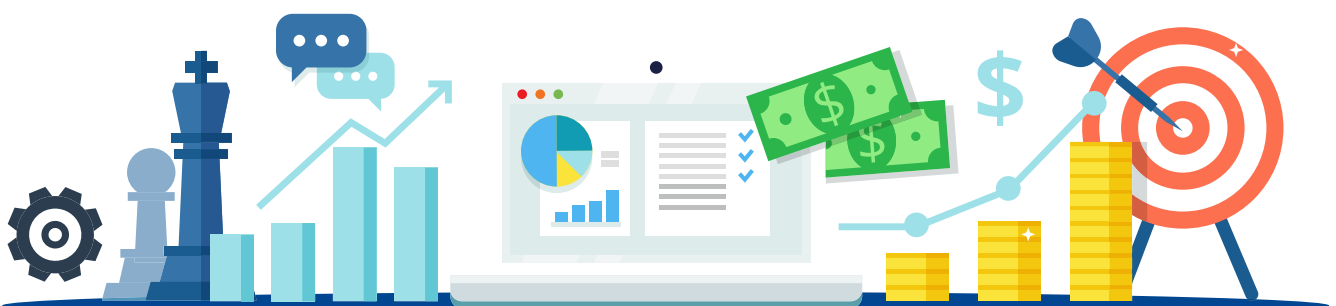
- The objective of allocating transaction price is for an entity to allocate transaction price to each performance obligation in an amount that depicts expected entitlement for transferring the promised goods or services
- The stand-alone selling price is the price at which an entity would sell a promised good or service separately to a customer. Entities should allocate the transaction price in proportion to the

stand-alone selling price of each distinct good or service (determined at contract inception). The stand-alone selling price is determined as below:

- * *Observable price:* The best evidence of a stand-alone selling price is the observable price of a good or service when the entity sells that good or service separately in similar circumstances and to similar customers,
- * *Estimated price:* If a stand-alone selling price is not directly observable, an entity should estimate it by considering all information available to the entity, maximise the use of observable inputs and apply estimation methods consistently in similar circumstances. Some of the estimation methods are:
 - > Adjusted market assessment approach
 - > Expected cost plus a margin approach
 - > Residual approach (only in limited circumstances).

• Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation

- Revenue is required to be recognised when (i.e. at a point in time) or as (i.e. over a period of time) the entity satisfies a performance obligation by transferring the control of a promised good or service to the customer.
- A performance obligation is satisfied over time if either:
 - * Customer simultaneously receives and consumes the benefits as the entity performs
 - * Customer controls the asset as the entity creates or enhances it
 - * The entity's performance does not create an asset with an alternative use and there is right to payment for performance to date.
- If a performance obligation is not satisfied over time, an entity satisfies the performance obligation at a point in time.
- Measurement of revenue is dependent upon the determination of the transaction price allocated to that performance obligation.



Other principles

• Contract costs

- Incremental costs of obtaining a contract with a customer are recognised as an asset, if they are expected to be recovered
- Costs incurred to fulfil a contract are generally recognised as an expense, however, in certain cases, they may be recognised as an asset.

• Presentation

- When either party to a contract has performed, depending on the relationship between the entity's performance and the customer's payment, a contract asset or a contract liability is presented in the balance sheet
- Any unconditional rights to consideration are separately presented as a receivable.

• Disclosures

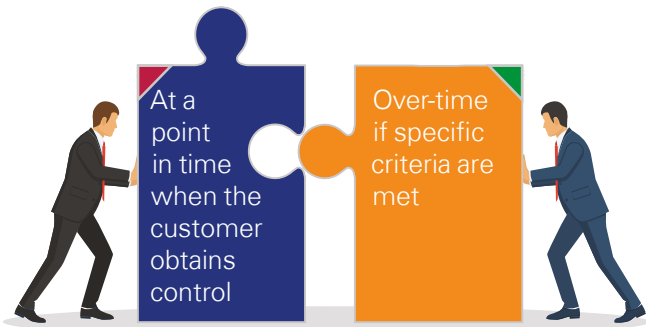
- The objective of the revenue disclosures is to enable users to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

Guidance from ITFG clarifications

Timing of revenue recognition

Ind AS 115 provides a control-based approach to be applied to all transactions at the contract inception. An entity needs to evaluate whether it transfers control of the good or service over-time or at a point in time for the purposes of recognising revenue.

Revenue is recognised...



Ind AS 115 provides that revenue is recognised over-time when any of the following criteria are met:

- Customer simultaneously receives and consumes the benefits provided as the entity performs
- Entity's performance creates or enhances an asset that the customer controls
- Entity's performance does not create an asset with an alternative use to it and it has an enforceable right to payment for performance completed to date.

Significant differences from IFRS¹

- IFRS 15, *Revenue from Contracts with Customers* provides that all types of penalties which may be levied in the performance of a contract should be considered in the nature of variable consideration for recognising revenue. Ind AS 115 excludes penalties from the list of variable consideration. Ind AS 115 has been amended to provide that penalties are required to be accounted for as per the substance of the contract. Where the penalty is inherent in determination of transaction price, it would form part of variable consideration, otherwise the same would not be considered for determining the consideration.
- Ind AS 115 requires an entity to present separately the amount of excise duty included in the revenue recognised in the statement of profit and loss. There is no such requirement in IFRS 15.
- Additional disclosures as compared to IFRS 15 are prescribed. An entity is required to present reconciliation of the amount of revenue recognised in the statement of profit and loss with the contracted price showing separately each of the adjustments made to the contract price specifying the nature and amount of each such adjustment separately.
- Additional guidance has been given in Ind AS 115 to explain the accounting treatment in case of transfers of control of a product to a customer with an unconditional right of return.



1. Indian Accounting Standards (Ind AS): An overview (Revised 2019) issued by ICAI.



If none of the above criteria are met, then control of the good or service transfers at a point in time.

In the above context, ITFG considered an issue relating to a shipping entity involved in transportation of petroleum products from one port to other.

The contracts with customers state that the contract would not be terminated once the entity takes delivery of goods from the customers at the port and sails to the designated port of destination. The following issues in respect of performance obligations under the contract were considered by the ITFG:

- i. Whether the performance obligation under the above contract is satisfied over time or at a point in time
- ii. In case the performance obligation under the above contract is satisfied over time, whether the extent of satisfaction of performance obligation could be measured on the basis of number of days the vessel has sailed.

Whether the performance obligation is satisfied over time or at a point in time

ITFG clarified that in the given case, the entity would need to evaluate its performance obligation to determine if it satisfies any of the requisite criterion.

For evaluating criteria (a), in the given case an entity may not be able to readily identify whether a customer simultaneously receives and consumes the benefits from its performance. The entity is required to evaluate whether another entity would need to substantially re-perform the work carried out by the entity to date. If that work would not need to be substantially re-performed, then revenue would be recognised over time.

Considering the nature of performance obligation of the entity, it would not be meeting criterion (b) as it would not be able to create or enhance an asset that the customer controls as the asset is created or enhanced.

In the given case, for evaluation of criterion (c), an entity should consider whether the performance obligation creates an alternative use to it. Additionally, in determining whether it has an enforceable right to payment for performance completed to date requires consideration of the detailed requirements and guidance provided in Ind AS 115.

Measurement of progress towards complete satisfaction of a performance obligation

Ind AS 115 specifies the following two types of methods for measuring progress based on the nature of the goods or services that the entity promised to transfer to the customer:

- Input method
- Output method.

Further, ITFG clarified that basis the above evaluation of criteria, if entity concludes that the performance obligation of the entity under its contract with a customer is satisfied over time, then the entity is required to determine an appropriate method of measuring progress on the basis of the relevant requirements and guidance contained in Ind AS 115. (*ITFG 19, Issue 2*)

First-time adopter of Ind AS transitional options under Ind AS 115

For existing Ind AS users Ind AS 115 provides two methods of accounting for transition - the retrospective method (with or without one or more of four practical expedients) and the cumulative effect method (simplified transition method).

In a situation where an entity (ABC Ltd.) complying with Ind AS for the first time from 1 April 2018 is required to comply with Ind AS 115, ITFG clarified that a first-time adopter does not have the choice of applying the simplified transition method.

Please refer to the Chapter 9, First-time adoption of Indian Accounting Standards for more details on the above issue (*ITFG 19, Issue 3*)

Accounting treatment of deferred tax adjustments recognised in equity on first-time adoption of Ind AS in accordance with Ind AS 101, First-time adoption of Indian Accounting Standards at the time of transition to Ind AS 115/116, Leases

Please refer to the chapter 9, First-time adoption of Ind AS for more details on the above issue (*ITFG 23, Issue 2*)

Applicability of Ind AS 115 to distribution of gifts

Revenue is accounted for in accordance with Ind AS 115, only in case the counterparty to the contract is a customer. Further, a contract should create enforceable rights and obligations.

In case the conditions regarding a legally enforceable 'contract' and 'customer' are not met, the transaction would not fall within the scope of Ind AS 115.

Please refer to the chapter 4, Tangible and intangible assets for more details on the above issue (*ITFG 22, Issue 4*)

Expected Credit Loss (ECL) on the amount due in the course of business from government

Please refer to the chapter 3, Financial instruments for more details on the above issue (*EAC opinion published in the October 2018 edition of the Journal 'The Chartered Accountant'*)

Refer to educational material on Ind AS 115, for the following issues/topics:

Issue number	Topic
1	Guidance on difference between the terms 'revenue' <i>vis-à-vis</i> 'income'
2	Applicability of Ind AS 115 to real estate developers
3	Applicability of Ind AS 115 to revenue from the extraction of mineral ore
4	Applicability of Ind AS 20 to export incentive received by a company registered as an export-oriented unit (Similar to ITFG 17, Issue 3)
5	Guidance on identification of customers in transactions involving multiple parties
6	Guidance on non-monetary exchanges between a print media advertisement for an electronic media advertisement
7	Applicability of Ind AS 115 to non-monetary exchanges without commercial substance
8	Applicability of Ind AS 115 to non-monetary exchanges with commercial substance
9	Applicability of Ind AS 115 to contracts involving non-monetary exchange for dissimilar goods or services
10	Guidance on identifying the contract in situations where a customer has liquidity issues and collection is not considered probable
11	Guidance on identifying the contract and recognising revenue in situations where a customer (with little experience in a highly competitive industry) pays a non-refundable deposit at inception of the contract and enters into a long-term financing agreement
12	Guidance on identifying the contract in situations of non-refundable deposit
13	Guidance on identifying the contract in situations of oral contract
14	Guidance on combination of contracts in situation to treat two contracts as a single contract
15	Guidance on contract modifications and accounting for change in prospective consideration
16	Guidance in contract modifications in different situations of change in period, costs and consideration
17	Identifying performance obligations in a contract to build a house
18	Identifying performance obligations in a contract subject to approval of designing and tooling
19	Identifying performance obligations in a contract involving licence to use entity's name
20	Identifying performance obligations in contract of a series of distinct goods
21	Determining the transaction price in case of collection of Goods and Services Tax (GST)
22	Determining the transaction price for financial statements <i>vis-à-vis</i> sales for GST purpose
23	Adjustment of revenue in case of allowance of probable discount
24	Determining the transaction price in case of retrospective reduction in price
25	Determining the transaction price in case of a financing component



26	Determining the transaction price when fees received to provide a loan commitment
27	Allocating the transaction price to performance obligations
28	Allocating the transaction price to sales incentives (cash and non-cash)
29	Allocating the transaction price to performance obligations in case of a discount
30	Allocating the transaction price to performance obligations and treatment of incentive
31	Accounting treatment of reward points
32	Allocating the transaction price in situations of separately identifiable performance obligations
33	Transfer of control in situations of raising an invoice or transfer of legal title
34	Recognising revenue when performance obligation is satisfied (dispatch and installation of goods)
35	Recognising revenue when performance obligation is satisfied over time
36	Recognising revenue in situations of non-refundable upfront fees and sales based monthly royalty income
37	Recognising revenue in situation of collection based on achievement of sales target by customer
38	Recognising revenue as and when entity satisfies each performance obligation (unused contracted call minutes in relation to telecommunication entity)
39	Recognising revenue as and when entity satisfies each performance obligation (broadband data services)
40	Recognising revenue as and when entity satisfies each performance obligation (sale contract based on prices linked to organised market)
41	Recognising revenue when entity satisfies each performance obligation (measurement of the outcome of the performance obligation)
42	Recognising revenue in situations of one-time upfront charges
43	Recognising revenue in situations of transfer of control of goods (when a transporter is involved and delivery terms are Cost, Insurance and Freight (CIF))
44	Recognising revenue in contract of payroll processing for a year with monthly payment
45	Recognising revenue by use of input method based on costs incurred to measure progress of performance obligation
46	Guidance on whether a 'contract asset' is a 'financial instrument'
47	Right to return in case of manufacturer and seller of garments to retailers
48	Guidance on bill-and-hold arrangements
49	Guidance on retention money on long term contracts (engineering and construction)
50	Guidance on an entity providing goods or services as a principal or acting as an agent
51	Guidance on accounting for repurchase agreements in which an entity enters into a contract with a customer for the sale of an equipment and the contract includes: <ul style="list-style-type: none"> • <i>Situation 1</i>: A call option that gives an entity a right to repurchase the equipment • <i>Situation 2</i>: A put option that creates an obligation for the entity to repurchase the equipment at the customers request.²

2. This issue has been analysed in light of Ind AS 115 and erstwhile Ind AS 17, Leases. Ind AS 17 has been superseded by Ind AS 116, Leases with effect from 1 April 2019. Accordingly, users should revisit this issue in light of guidance provided under Ind AS 116.

Issue number	Topic
52	Guidance for an Asset Management Company (AMC) in situation of variable consideration
53	Guidance in situations where manufacturer enters into a consignment agreement with a retailer
54	Information of contract to be included in disclosure of the transaction price allocated to the remaining performance obligations as per requirements of Ind AS 115
55	Guidance on whether disaggregated revenue disclosure always would be at the same level as its segment disclosures
56	Guidance on presentation of advance from customer
57	Guidance on treatment of cost of obtaining contracts in situations of discretionary annual bonus to employees and other costs
58	Guidance on differential sales commission to employees based on their designations to be treated as costs of obtaining contracts
59	Guidance on training expenses to be treated as cost of fulfilling contracts
60	Guidance on transition requirements under modified retrospective approach
61	Guidance on difference in accounting for revenue on transition to Ind AS 115
62	Guidance on software license to be treated as a distinct performance obligation or bundled with implementation services
63	Guidance on software licence to be treated as a distinct performance obligation or bundled with customisation services in certain scenarios
64	Revenue recognition in case of a Software-as-a-Service (SaaS) provider
65	Guidance on identification of licence as a distinct performance obligation from that of the hosting contract in different situations
66	Guidance on whether SaaS software and other services are distinct performance obligations
67	Guidance on whether anti-virus software and updates be distinct performance obligations
68	Guidance on accounting for sales commission to obtain a contract
69	Guidance on tooling cost incurred in fulfilling a contract with customer
70	Identification of contract in case of a real estate industry
71	Identifying performance obligation in real estate entity
72	Identifying performance obligation in situation of mall management and leasing services
73	Guidance on separate performance obligations in case of real estate industry
74	Measurement of transaction price in case of revenue recognised over a period by a real estate developer
75	Determination of significant financing components in contract for construction of a building
76	Revenue recognition in case of real estate developer in certain scenarios
77	Measuring progress of revenue by a real estate developer
78	Revenue recognition in situation of sale of multi-storied apartment building in stages

