



IFRS 15; Revenue from contracts with customers

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- The following discussions and examples do not necessarily represent Deloitte Touche Tohmatsu policy with respect to the issues raised
- The outcome of any independent situation depends upon the specific facts and circumstances in which the issue arises and on the interpretation of IFRS
- The views expressed cannot be relied upon as accounting advice
- Check with your advisor/auditor/management before taking action



Agenda

Overview

The revenue model:

- Identify the contract(s) with the customer
- Identify the performance obligations in the contract
- Determine the transaction price
- Allocate the transaction price to the performance obligation
- Recognise revenue when (or as) the entity satisfies a performance obligation

Disclosures

COVID-19 Considerations

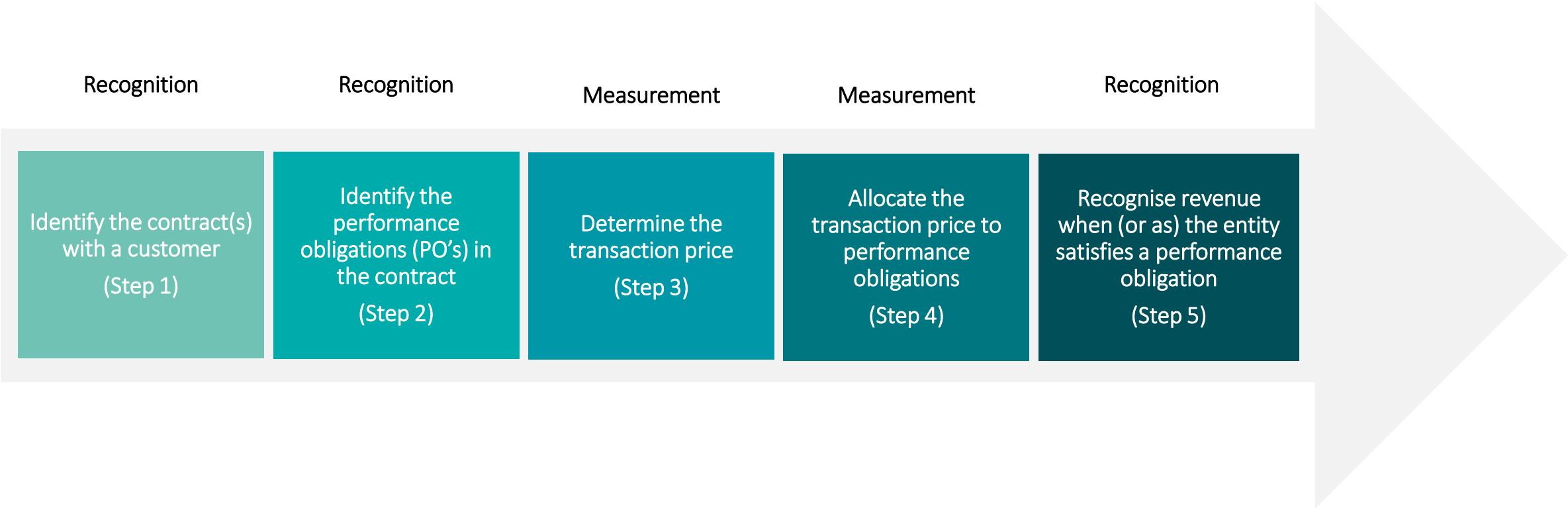


Overview.

- The Standard applies to an **individual contract** with a customer.
- IFRS 15 replaced all of the legacy revenue standards and interpretations in IFRS, including IAS 11 Construction Contracts, IAS 18 Revenue, IFRIC 13 Customer Loyalty Programmes, IFRIC 15 Agreements for the Construction of Real Estate, IFRIC 18 Transfers of Assets from Customers and SIC-31 Revenue – Barter Transactions Involving Advertising Services (legacy revenue requirements or legacy IFRS).
- IFRS 15 became effective for annual reporting periods beginning on or after 1 January 2018.
- Culmination of joint IASB/FASB project ; Generally converged with U.S. GAAP with some differences
- Establishes a single, comprehensive framework for revenue recognition and enhanced comparability
- Addresses inconsistencies and weaknesses in previous revenue standards and inadequate disclosure requirements
- Why is it a big deal?
- ✓ Entities are required to make many estimates and use judgement to apply the standard
- ✓ The impact of COVID-19 could increase the level of estimation

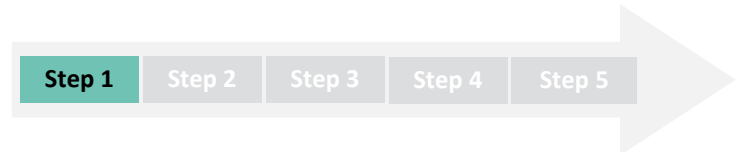
2. The revenue model

Core principle – Recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration the entity expects to be entitled in exchange for those goods or services.



The revenue model (cont'd)

Step 1 – Identify the contract



Contract defined as an agreement between two or more parties that creates enforceable rights and obligations

Criteria must be met for arrangement to be within scope of IFRS 15:

- Contract must be approved: Could be written, oral or implied : Does not exist if each party can unilaterally cancel without penalty
- Contract has commercial substance
- Parties have agreed to terms and are committed to perform
- Payment terms can be identified, and collection is probable(explained in the next slide)

These criteria are assessed at inception of the contract; If not met, should be continuously reassessed

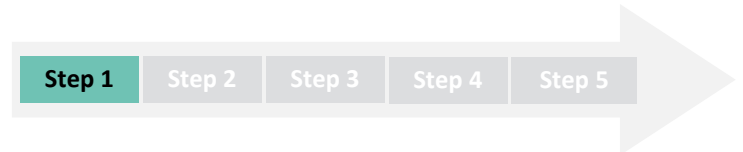
Multiple contracts entered into at the same time with the same customer should be combined if certain conditions are met

Modifications treated as a separate contract or part of the original contract, depending on what is modified



The revenue model (cont'd)

Step 1 – Identify the contract((cont'd)



Collectability:

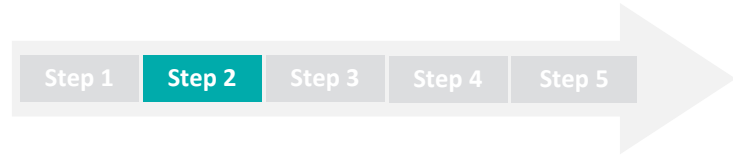
In evaluating whether collectability of an amount of consideration is **probable**, an entity shall consider only the customer's **ability and intention** to pay that amount of consideration when it is due.

The term probable is consistent with the existing definition more likely than not if not in IFRS

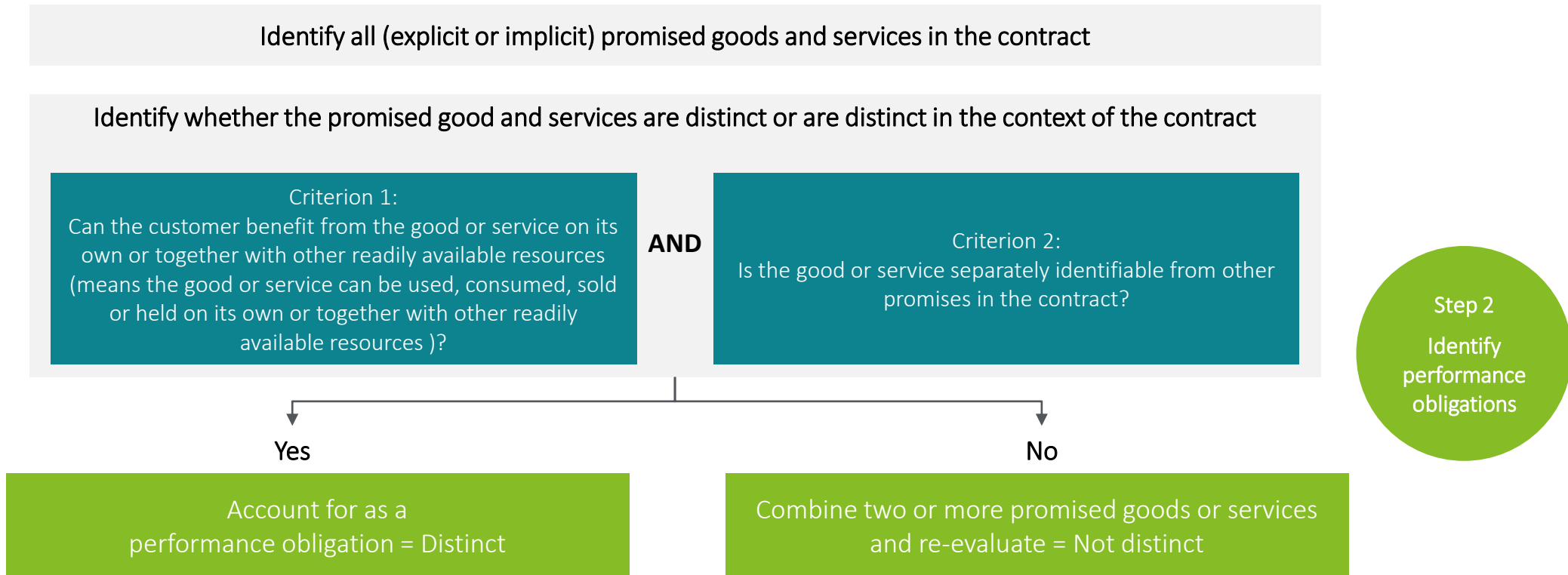
IFRS 15 Vs IFRS 9 Price Concession

The revenue model (cont'd)

Step 2 – Identify performance obligations

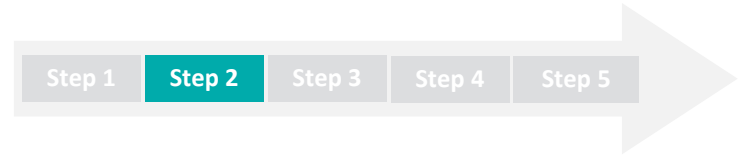


A performance obligation is a promise to transfer to the customer a good or service (or a bundle of goods or services) that is **distinct** or a **series of distinct goods or services**. These promises may not be limited to those explicitly included in written contracts.

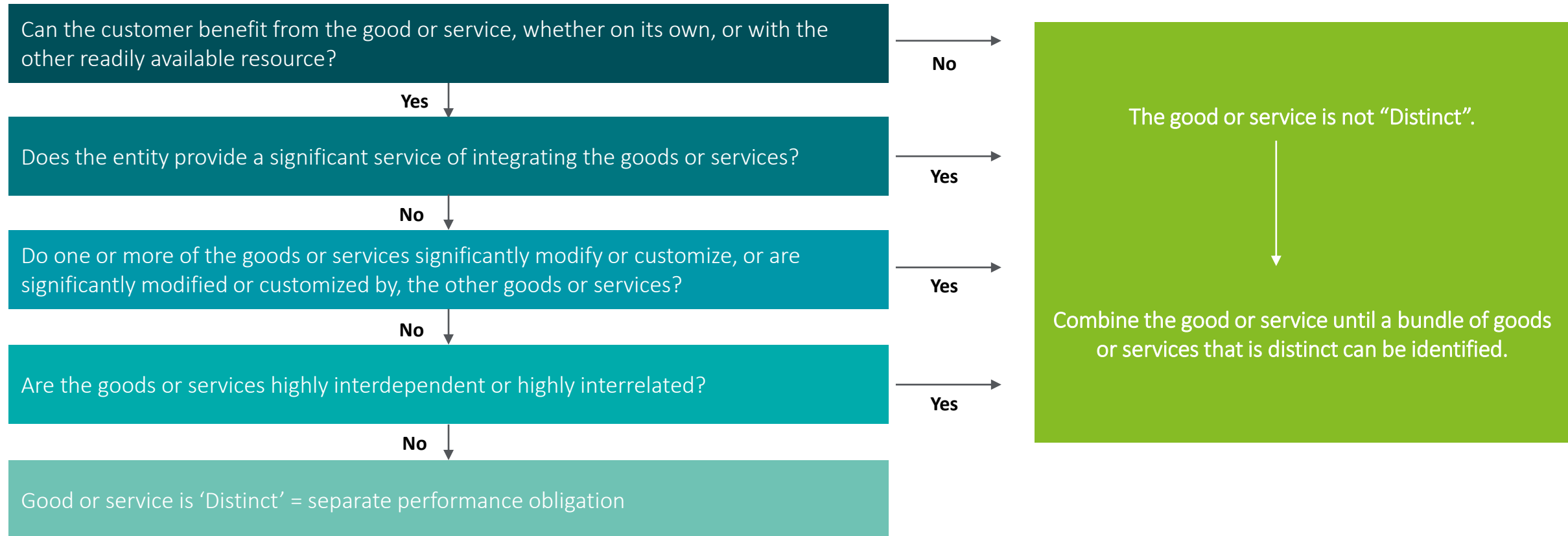


The revenue model (cont'd)

Step 2 – Identify performance obligations



If a promised good or service is **not distinct**, an entity shall combine that good or service with other promised goods or services until it identifies a bundle of goods or services that is distinct.



The revenue model (cont'd)

Step 2 – Identify performance obligations: Application guidance and other matters

Principal vs Agent

- When another party is involved in providing goods or services to a customer, an entity evaluates the nature of its promise to the customer.
- Entities must determine whether they are a principal or agent for each specified good or service.
- If an entity has control of a specified good or service before it is transferred to the customer, the entity is presumed to be the principal.

Principal

- Nature of promise is **to provide** goods or services itself.
- Control of the promised good or service prior to transfer to customer should not simply be **momentary legal title** prior to transfer.
- Indicators of being a principal are met
 - ✓ The entity is primarily responsible for fulfilling the promise
 - ✓ The entity has inventory risk
 - ✓ The entity has discretion in establishing the price

Recognise revenue in gross amount

Agent

- Nature of promise is **to arrange** for the other party to provide the goods or services.
- Does **not control** promised good or service **before it is transferred** to customer.

Recognise revenue in net amount

The revenue model (cont'd)

Step 3 – Determine the transaction price



Principle: The 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 the amount collected on behalf of third parties (i.e., taxes).

Transaction price shall include:

- Fixed consideration
- Variable consideration
- Constraining estimates of variable consideration
- The existence of a significant financing component in the contract
- Non-cash consideration; and
- Consideration payable to a customer



The revenue model (cont'd)

Step 3 – Determine the transaction price



Variable consideration

The definition of variable consideration is broad as the consideration is susceptible to other factors and events; Common types of events that may cause consideration to be variable are bonuses, discounts, rebates, refunds, credits, price concessions, incentives returns, penalties and other similar items.

Assuming entity has sufficiently reliable data on which to base an estimate, the transaction price is estimated using the technique that better predicts the amount an entity will be entitled to:

Expected value: Sum of the probability-weighted amounts in a range of possible outcomes

Most Likely amount; The single most likely amount in a range of possible outcomes

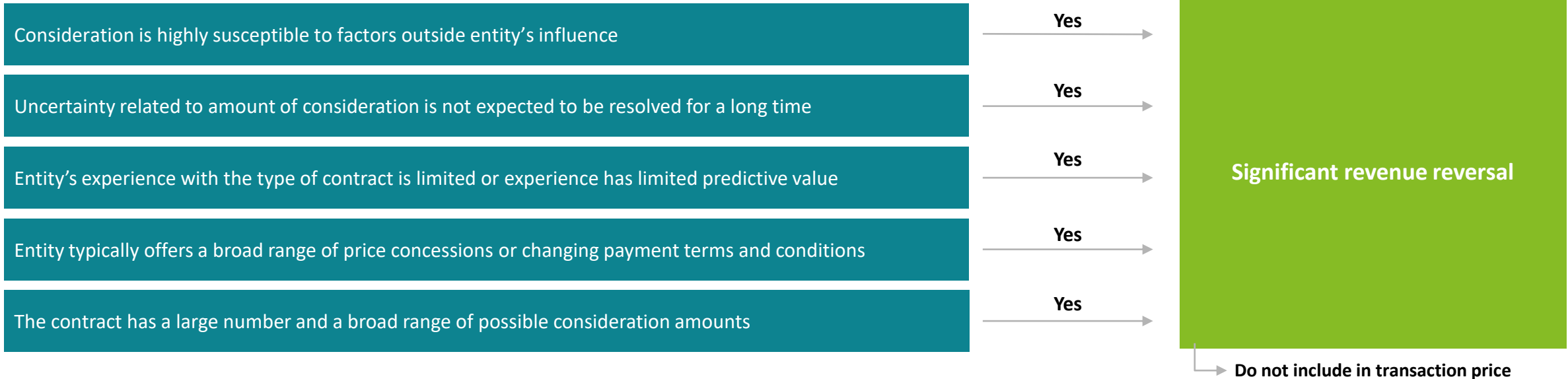
The revenue model (cont'd)

Step 3 – Determine the transaction price



Constraint on variable consideration

- Required to evaluate whether to ‘constrain’ amounts of variable consideration included in transaction price
- An entity shall include in the transaction price some or all of an amount of variable consideration estimated only to the extent that it is **highly probable** that a **significant reversal** in the amount of cumulative revenue recognized **will not occur** when the uncertainty associated with the variable consideration is subsequently resolved.
- Need to assess the **likelihood** and **magnitude** to determine the probability of a significant reversal.
- Consider the following factors:



The revenue model (cont'd)

Step 3 – Determine the transaction price



Refund Liability /Right of Return

- An entity shall Recognise a refund liability if the entity receives consideration from a customer and expects to refund some or all of that consideration to the customer.
- A refund liability is measured at the amount of consideration received (or receivable) for which the entity does not expect to be entitled (ie amounts not included in the transaction price).

The refund liability should be updated at the end of each reporting period for changes in circumstances.

Significant financing component

Adjustment to transaction price is done when the pricing purpose is to provide financing

- Practical expedient: Not required if payment terms are less than a year
- Significance is assessed at contract level and not at portfolio level

An entity shall present the effects of financing (interest revenue or interest expense) separately from revenue from contracts with customers in the statement of comprehensive income

The revenue model (cont'd)

Step 4 – Allocate the transaction price



- **Allocate the transaction price to each performance obligation** based on the stand-alone price
- **SSP** - is the price at which an entity would sell a promised good or service separately to a customer. It can be: the observable price, a contractually stated price or a list price
- If a stand-alone selling price is not directly observable, an entity shall estimate the SSP
 - Suitable methods for estimating the stand-alone selling price of a good or service include, but are not limited to:

Expected cost-plus margin

Adjusted market assessment

Residual approach

- Stand alone prices selling prices used to perform allocation are not updated after contract inception



The revenue model (cont'd)

Step 5 – Recognise revenue



An entity recognizes revenue **when or as** the entity **satisfies a performance obligation** by **transferring** a promised good or service (ie an asset) to a customer. An asset is **transferred** when or as the customer obtains **control** of that asset.

Control

- The ability to direct the use of,
- And obtain substantially all of the remaining benefits from, the asset

Control includes the ability to prevent other entities from directing the use of, and obtaining the benefits from, an asset.



The revenue model (cont'd)

Step 5 – Recognise revenue

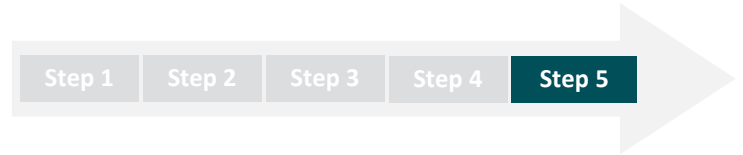


For performance obligations satisfied **at a point in time**, indicators of the transfer of control include, but are not limited to, the following:

- 1 Entity has a **present right to payment** for the asset
- 2 The customer has **legal title** to the asset
- 3 The entity has **transferred physical possession** of the asset
- 4 The customer has the **significant risks and rewards** of ownership of the asset
- 5 The customer has **accepted** the asset

The revenue model (cont'd)

Step 5 – Recognise revenue



- For each performance obligation in a contract, an entity first determines whether the **performance obligation is satisfied over time** – i.e. control of the good or service transfers to the customer over time.
- Evaluate if control of a good or service transfers over time, **if not**, then control transfers at **a point in time**.
- An entity satisfies a performance obligation over time if:

The customer simultaneously receives and consumes the benefits provided by the entity – routine or recurring services.
(e.g., cleaning service)

or

The entity's performance creates or enhances an asset that the customer controls as the asset is created or enhanced.
(e.g., Building an asset on a customer's site)

or

Performance does not create an asset with an **alternative use** and the entity has an **enforceable right to payment** for performance completed to date. (e.g., Building a specialized asset that only the customer can use or building an asset to a customer's specifications)

Presentation

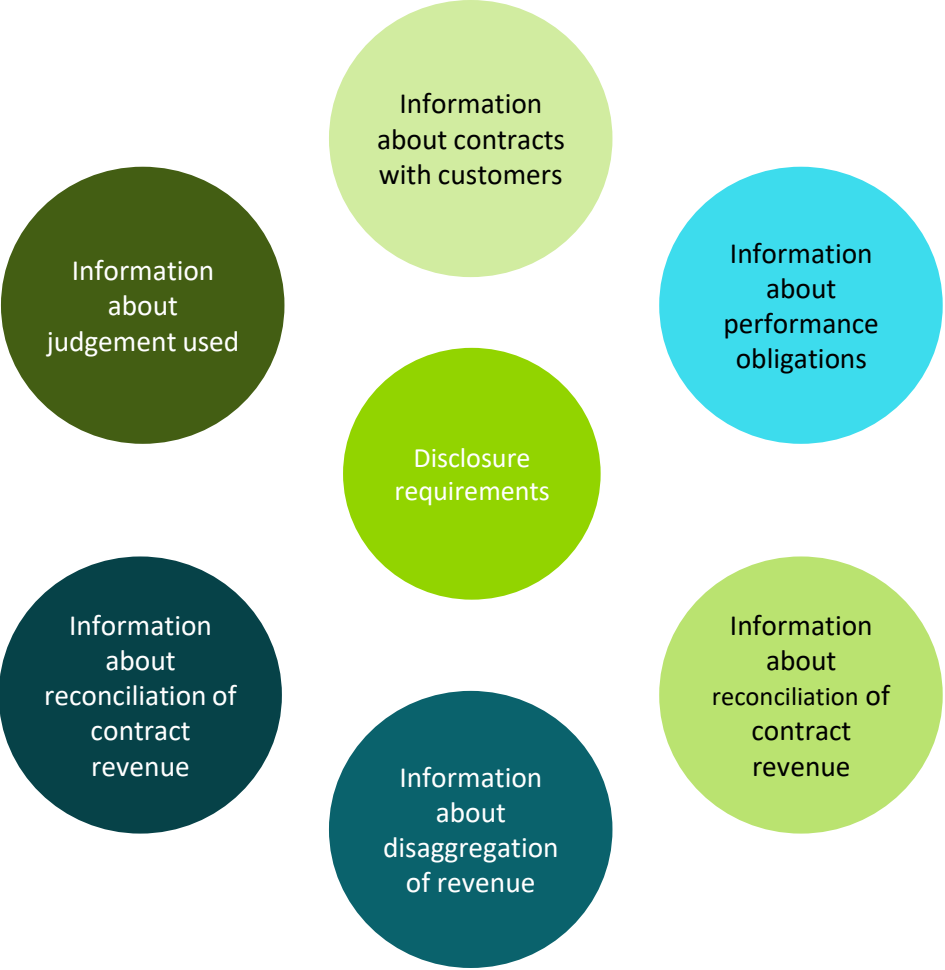
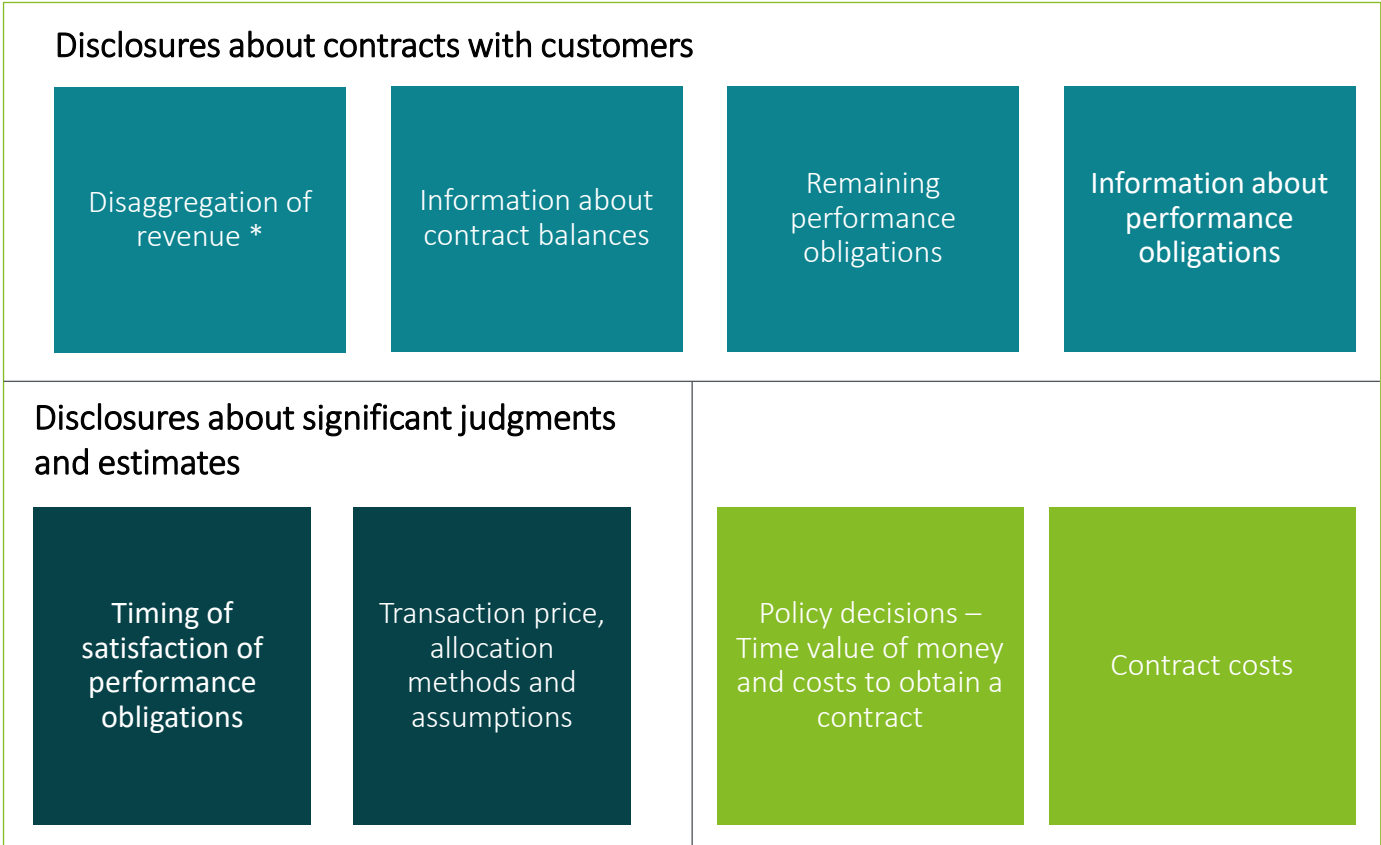
Annual disclosure

- An entity shall present the contract in the statement of financial position as a **contract asset or a contract liability**, depending on the relationship between the entity's performance and the customer's payment.
- An entity shall present any **unconditional rights to consideration separately as a receivable**.
- 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.
- If an entity performs by transferring goods or services to a customer before the customer pays consideration or before payment is due, the entity shall present the contract as a contract asset, excluding any amounts presented as a receivable, and assess the contract asset for impairment in accordance with IFRS 9.

Disclosure

The standard contains both qualitative and quantitative disclosure requirements for annual and interim periods.

The standard requires the disaggregation of revenue from contracts with customers into categories that depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors and includes examples of these categories.



Disclosure

The standard contains both qualitative and quantitative disclosure requirements for annual and interim periods.

Annual disclosure

- The objective of the disclosure requirements is for an entity to disclose sufficient information to enable users of the financial statements to understand the **nature, amount, timing and uncertainty of revenue and cash flows** arising from contracts with customers.
- An entity shall aggregate or disaggregate disclosures so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items that have substantially different characteristics.
 - Revenue recognized from contracts with customers and any impairment losses recognized on receivables or contract assets arising from contracts with customers.
 - If an entity elects either the practical expedient not to adjust the transaction price for a significant financing component or the practical expedient not to capitalize costs incurred to obtain a contract, then it discloses this fact.
 - The standard includes disclosure requirements on the **disaggregation** of revenue into categories
- Contract balances, information and timing of satisfaction of its performance obligations, transaction price allocated to the remaining performance obligations, significant judgements, assets recognized to obtain or fulfil a contract and practical expedients elected.

COVID-19 Impact; Disclosures

IFRS 15 has extensive disclosure requirements but in current times there is an even greater need to tell a clear story and explain associated uncertainties. Below are some of the specific disclosures that might need to be enhanced, but please note that this is not a comprehensive list.

- Revenue recognised in the current period in relation to performance obligations satisfied in previous periods. Typically, this is the effect of releasing variable consideration that has previously been constrained and the amount may be negative for some entities.
- Changes to typical timing of payment / payment terms, and impact on contract assets and liabilities.
- Explanation of significant changes to contract assets and liabilities, including quantitative information on key impacts.
- Significant judgements, and changes in judgements, relating to:
 - ✓ assessing when control is transferred to customer;
 - ✓ estimating variable consideration;
 - ✓ constraining estimates of variable consideration;
 - ✓ measuring obligations for returns, refunds and similar obligations.



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