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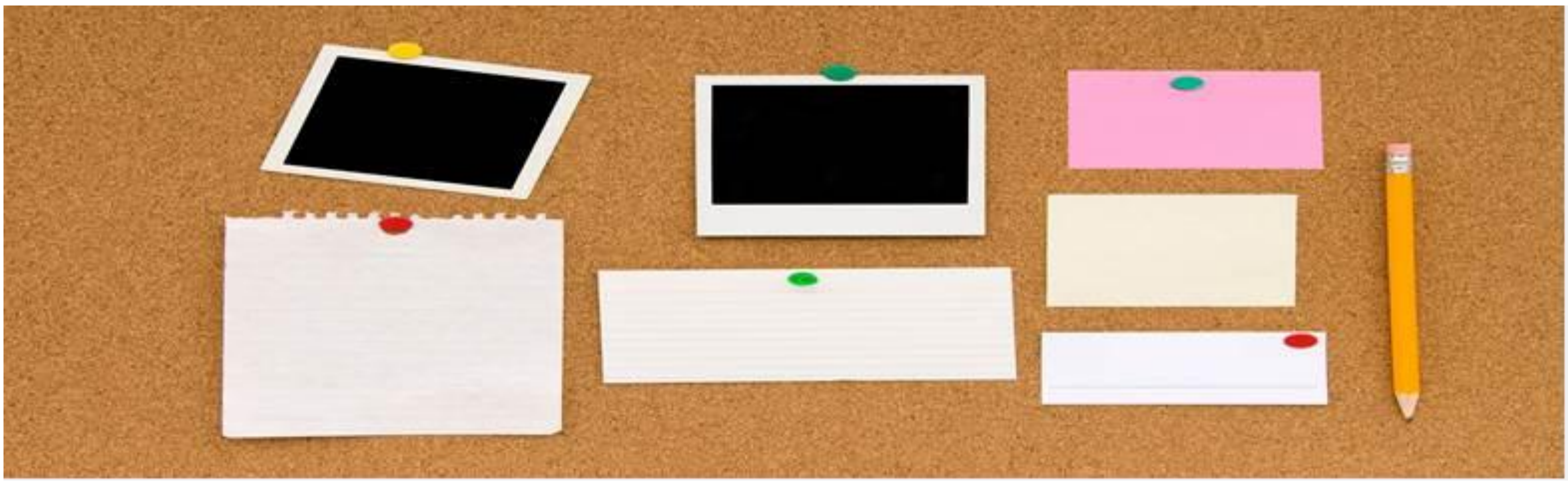

Accounting & Auditing News

IFRS 15 — *Revenue from Contracts with Customers*: Part 2C – Differences vs. Revenue Related Interpretations

Revenue Recognition

Under IFRIC 13, *Customer Loyalty Programmes* *(IFRIC 13.5-9)*

The fair value of the consideration received or receivable in respect of the initial sale shall be allocated between the award credits and the other components of the sale. *(IFRIC 13.5)*

The consideration allocated to the award credits shall be measured by reference to their fair value, ie the amount for which the award credits could be sold separately. *(IFRIC 13.6)*

If the entity supplies the awards itself, it shall recognize the consideration allocated to award credits as revenue when award credits are redeemed and it fulfils its obligations to supply awards. The amount of revenue recognized shall be based on the number of award credits that have been redeemed in exchange for awards, relative to the total number expected to be redeemed. *(IFRIC 13.7)*

Under IFRS 15, *Revenue from Contracts with Customers* *(IFRS 15.B39-B43)*

If, in a contract, an entity grants a customer the option to acquire additional goods or services, that option gives rise to a performance obligation in the contract only if the option provides a material right to the customer that it would not receive without entering into that contract. If the option provides a material right to the customer, the customer in effect pays the entity in advance for future goods or services and the entity recognizes revenue when those future goods or services are transferred or when the option expires. *(IFRS 15.B40)*

If a customer has the option to acquire an additional good or service at a price that would reflect the stand-alone selling price for that good or service, that option does not provide the customer with a material right even if the option can be exercised only by entering into a previous contract. In those cases, the entity has made a marketing offer that it shall account for in accordance with this Standard only when the customer exercises the option to purchase the additional goods or services. *(IFRS 15.B41)*

Paragraph 74 requires an entity to allocate the transaction price to performance obligations on a relative stand-alone selling price basis. If the stand-alone selling price for a customer's option to acquire additional goods or services is not directly observable, an entity shall estimate it. That estimate shall reflect the discount that the customer would obtain when exercising the option, adjusted for both of the following: *(IFRS 15.B42)*

(a) any discount that the customer could receive without exercising the option; and

(b) the likelihood that the option will be exercised.

If a customer has a material right to acquire future goods or services and those goods or services are similar to the original goods or services in the contract and are provided in accordance with the terms of the original contract, then an entity may, as a practical alternative to estimating the stand-alone selling price of the option, allocate the transaction price to the optional goods or services by reference to the goods or services expected to be provided and the corresponding expected consideration. Typically, those types of options are for contract renewals. *(IFRS 15.B42)*

Analysis of the Change

IFRIC 13.6 states that award credits should be measured "by reference to their fair value" (emphasis added). But it does not mandate any particular method for allocating amounts to the award credits. Whereas, IFRS 15.74 requires an entity to allocate the transaction price to performance obligations on a relative stand-alone selling price basis. This shows that IFRS 15 is much more prescriptive than IFRIC 13.

Timing of Revenue Recognition

Under IFRIC 15, *Agreements for the Construction of Real State* *(IFRIC 15.10-12)*

The fundamental issue is whether the developer is selling a product (goods) – the completed apartment or house – or is selling a service – a construction service as a contractor engaged by the buyer. Revenue from selling products is normally recognized at delivery. Revenue from selling services is normally recognized on a percentage-of-completion basis as construction progresses.

Determining whether an agreement for the construction of real estate is within the scope of IAS 11 or IAS 18 depends on the terms of the agreement and all the surrounding facts and circumstances. Such a determination requires judgment with respect to each agreement. *(IFRIC 15.10)*

IAS 11 applies when the buyer is able to specify the major structural elements of the design of the real estate before construction begins and/or specify major structural changes once construction is in progress (whether or not it exercises that ability). When IAS 11 applies, the construction contract also includes any contracts or components for the rendering of services that are directly related to the construction of the real estate in accordance with paragraph 5(a) of IAS 11 and paragraph 4 of IAS 18. *(IFRIC 15.11)* In such a case, the revenue is recognized over time.

In contrast, an agreement for the construction of real estate in which buyers have only limited ability to influence the design of the real estate, eg to select a design from a range of options specified by the entity, or to specify only minor variations to the basic design, is an agreement for the sale of goods within the scope of IAS 18. *(IFRIC 15.12).* In such a case, the revenue is recognized at a point in time.

Under IFRS 15, Revenue from Contracts with Customers *(IFRS 15.31-45)*

An entity shall recognize 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. *(IFRS 15.31)*

An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognizes revenue over time, if one of the following criteria is met: *(IFRS 15.35)*

a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);
b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or
c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37). *(IFRS 15.31)*

If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. *(IFRS 15.38)*

Analysis of the Change

Some entities may find that revenue previously recognized at a point in time should now be recognized over time, or vice versa. Whether revenue should be recognized over time or at a point in time will often depend on a careful analysis of specific contract terms. In determining whether revenue is recognized at a point in time or over time, it is important for an entity to consider the following factors:

- Careful assessment whether the entity could have an alternative use for the asset under construction and the entitlement of the entity to be paid for the work perform to date.
- It is important to focus on any contractual terms allowing the customer to cancel, curtail or significantly modify the contract and whether if such circumstances arose, the seller would always be contractually entitled to adequate compensation for work performed to date.

Assessment of these factors, and others will need to be made in the context of both the contract terms and the local legal government.

Where an entity concludes that revenue should be recognized over time, it will need to consider how to measure progress towards complete satisfaction of performance obligations. IFRS 15 specifies that the measure of progress shall exclude any goods or services for which the entity does not transfer control to the customer. As such, the measure of progress (and therefore the percentage of revenue to be recognized) may be affected by whether or not control of the land on which property is being constructed is transferred to the buyer (and the timing of that transfer) when assessing the extent to which their accounting policy for revenue may need to be amended.

Additional differences may still be identified upon actual implementation of the standard. The Philippine Interpretations Committee has formed a project team to study the impact of IFRS 15 in relation to the deferral of IFRIC 15 focusing on real estate industry.

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