

UDHNA COLLEGE

M. COM.-I

FINANCIAL & MANAGEMENT ACCOUNTING-I

UNIT-3 Indian Accounting Standard (Ind AS) 115 Revenue from Contracts with Customers (15%)

- **Objective:**

This standard establishes principles to report useful information about the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer. The core principle is that an entity shall recognise 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. The standard specifies the accounting for an individual contract with a customer. However, as a practical expedient, an entity may apply this Standard to a portfolio of contracts (or performance obligations) with similar characteristics if the entity reasonably expects that the effects of applying the Standard to the portfolio would not differ materially from applying this Standard to the individual contracts (or performance obligations) within that portfolio.

- **Scope:**

The standard applies to all contracts with customers, except the following:

- (a) lease contracts within the scope of Ind AS 17, Leases;
- (b) insurance contracts within the scope of Ind AS 104, Insurance Contracts;
- (c) financial instruments and other contractual rights or obligations within the scope of Ind AS 109, Financial Instruments, Ind AS 110, Consolidated Financial Statements, Ind AS 111, Joint Arrangements, Ind AS 27, Separate Financial Statements and Ind AS 28, Investments in Associates and Joint Ventures; and
- (d) non-monetary exchanges between entities in the same line of business to facilitate sales to customers or potential customers. For example, this Standard would not apply to a contract between two oil companies that agree to an exchange of oil to fulfil demand from their customers in different specified locations on a timely basis.

Ind AS 115 applies only if the counterparty to a contract is a customer. A customer is 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.

A counterparty to the contract would not be a customer if, for example, the counterparty has contracted with the entity to participate in an activity or process in which the parties to the contract share in the risks and benefits that result from the activity or process (such as developing an asset in a collaboration arrangement) rather than to obtain the output of the entity's ordinary activities.

- **Recognition:**

Identifying the contract An entity shall account for a contract with a customer only when all of the following criteria are met:

- (a) the parties to the contract have approved the contract (in writing, orally or in accordance with other customary business practices) and are committed to perform their respective obligations;
- (b) the entity can identify each party's rights regarding the goods or services to be transferred;
- (c) the entity can identify the payment terms for the goods or services to be transferred;
- (d) the contract has commercial substance (ie the risk, timing or amount of the entity's future cash flows is expected to change as a result of the contract); and
- (e) it is probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. 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 amount of consideration to which the entity will be entitled may be less than the price stated in the contract if the consideration is variable because the entity may offer the customer a price concession.

A contract is an agreement between two or more parties that creates enforceable rights and obligations. Enforceability is a matter of law. Contracts can be written, oral or implied by an entity's customary business practices. For the purpose of applying this Standard, a contract does not exist if each party to the contract has the unilateral enforceable right to terminate a wholly unperformed contract without compensating the other party (or parties).

If a contract meets the criteria (mentioned above) at contract inception, then an entity shall not reassess those criteria unless there is an indication of a significant change in facts and circumstances. If it does not meet the criteria, then an entity shall continue to assess the contract to determine whether the criteria are subsequently met.

When a contract does not meet the given criteria and an entity receives consideration from the customer, then it shall recognise the consideration received as revenue only when either of the following events has occurred:

- (a) the entity has no remaining obligations to transfer goods or services to the customer and all, or substantially all, of the consideration promised by the customer has been received by the entity and is non refundable; or
- (b) the contract has been terminated and the consideration received from the customer is non-refundable.

- **Contract modification:**

A contract modification is a change in the scope or price (or both) of a contract that is approved by the parties to the contract. It shall be accounted for as a separate contract if both of the following conditions are present:

- (a) the scope of the contract increases because of the addition of promised goods or services that are distinct; and
- (b) the price of the contract increases by an amount of consideration that reflects the entity's stand-alone selling prices of the additional promised goods or services and any appropriate adjustments to that price to reflect the circumstances of the particular contract.

If contract modification is not accounted for as a separate contract, then an entity shall account for the promised goods or services not yet transferred at the date of the contract modification (i.e. the remaining promised goods or services) in whichever of the following ways is applicable:

- (a) account for as if it were a termination of the existing contract and the creation of a new contract, if the remaining goods or services are distinct from the goods or services transferred. The amount of consideration to be allocated is the sum of:
 - (i) the consideration promised by the customer (including amounts already received from the customer) that was included in the estimate of the transaction price and that had not been recognised as revenue; and
 - (ii) the consideration promised as part of the contract modification.
- (b) account for as if it were a part of the existing contract if the remaining goods or services are not distinct and, therefore, form part of a single performance obligation that is partially satisfied at the date of the contract modification.
- (c) If the remaining goods or services are a combination of items (a) and (b), then the effects of the modification on the unsatisfied (including partially unsatisfied) performance obligations in the modified contract shall be accounted for in a manner that is consistent with the objectives of this paragraph.

- **Satisfaction of performance obligations:**

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

For each performance obligation identified, determine at contract inception whether it satisfies the performance obligation over time or at a point in time. If an entity does not satisfy a performance obligation over time, the performance obligation is satisfied at a point in time.

- **Performance obligations satisfied over time:**

A performance obligation is satisfied over time, if one of the following criteria is met: (a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs;

(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; or

(c) the entity's performance does not create an asset with an alternative use to the entity and the entity has an enforceable right to payment for performance completed to date.

For some types of performance obligations, assessment of (a) above would be straightforward. For other types, 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 those circumstances, 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 assessing whether an asset has an alternative use to an entity, an entity shall consider the effects of contractual restrictions and practical limitations on the entity's ability to readily direct that asset for another use, such as selling it to a different customer. A contractual restriction must be substantive i.e. a customer could enforce its rights to the promised asset if the entity sought to direct the asset for another use.

An entity has a right to payment for performance completed to date if it gets an amount that would compensate an entity for performance completed to date which is an amount that approximates the selling price of the goods or services transferred to date (for example, recovery of the costs incurred by an entity in satisfying the performance obligation plus a reasonable profit margin) rather than compensation for only the entity's potential loss of profit if the contract were to be terminated.

For each performance obligation satisfied over time recognise revenue over time by measuring the progress towards complete satisfaction of that performance obligation. Appropriate methods of measuring progress include output methods and input methods. In determining the appropriate method entity shall consider the nature of the good or service that the entity promised to transfer to the customer.

Output methods recognise 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.

Input methods recognise 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.

Measurement:

When (or as) a performance obligation is satisfied, recognise as revenue the amount of the transaction price (which excludes estimates of variable consideration that are constrained) that is allocated to that performance obligation.