Financial Reporting Faculty, ICAN

Hello!

- This is an IFRS Training video that addresses IFRS 15 (Revenue from contract with customers).
- As you are probably aware, the Standard had an effective date of 1st January 2018; which presupposes any entity that is IFRS compliant would have implemented systems and processes, including human capacity building to facilitate IFRS 15 adoption.
- This video is a summary clip that provides expose into the world of IFRS 15. I encourage you to buy the subscription to view the full version of the training video and much more from the Institute of Chartered Accountants of Nigeria.
- But first, a brief introduction about myself:
  - My name is Bolaji Osho, many know me as SENATOR
  - I am a Fellow of the Institute of Chartered Accountants of Nigeria.
  - All I do with my life is Financial Reporting training and consulting covering IFRS and IPSAS.
- Now to the subject matter, a question that many ask me quite regularly is why IFRS 15 and why did we have to change to IFRS 15?
- Because of time constraint, I am going to answer the question from 4 perspectives, of course there are a lot more but let us limit it to this 4 for now:

  - <u>Revenue Standard Proliferation:</u> To start with, IFRS 15 provides a single consistent authoritative source of reference with respect

to the nature, amount, timing and uncertainties of revenue and cashflows associated with revenue; whereas prior to the adoption of IFRS 15, a financial reporting practitioner/auditor needed to know six IFRS references in order to have full appreciation of the timing of revenue recognition and measurement. These IFRS authorities were IAS 18 (Revenue), IAS 11 (Construction contract), SIC 31 (Revenue, Barter transaction involving advertising services) IFRIC 13 (Customer Loyalty Programme), IFRIC 15 (Agreement for the construction of real estate), IFRIC 18 (Transfer of Assets to customers). With IFRS 15, we no longer have the needless proliferation of Standards. See IFRS 15 IN3 and IFRS 15 App. C10

- <u>Treatment of forfeited advance payments by customers:</u> Many players in the FMCG industry have policies that involve advance payment for product by their trade partners. I was facilitating an IFRS 15 training for a multinational in the downstream oil sector and a senior manager at the training asked me the question of what to do with advance payment made by wholesalers many years back that have now been forfeited on account of time expiry. Clearly, none of the legacy Revenue Standard provided any guidance on this popular case. Of course, such amount would initially have been recognized as liabilities (deferred income) and ultimately would be written off to the Statement of comprehensive income as goods are delivered or services provided. In practice, there are many approaches to this; let me share just four approaches with you:
  1. Write it off to other income i.e.
     - i. Dr: Deferred income,
     - ii. Cr: Other income
  2. Use it to reduce a cost i.e.

i. Dr: Deferred income,
ii. Cr: Cost of sale (for example)

3. Write it off to Revenue i.e.
    i. Dr: Deferred income,
    ii. Cr: Revenue.
4. The extreme approach is to credit retained earnings directly i.e.
    i. Dr: Deferred income
    ii. Cr: Retained earnings.

In the past, treatment of such forfeited advance payments varied widely and as indicated above due to the lack of guidance from the legacy revenue Standards. However, IFRS 15 refers to such liabilities as **brokerage** (IFRS 15 App. B45) and is quite categorical that such amount be recognized as Revenue (see IFRS 15 App. B46) of course after constraining them using IFRS 15 p. 56,57.

- <u>Expense or capitalize related expenses</u>: IAS 18, Revenue p. 14e, 20d make cost recognition and measurement conditions for recognizing revenue. IAS 18 p. 19 further reinforced the concept of matching. A careful assessment of those paragraphs could be misconstrued to mean certain PPPE items are written off to profit or loss if they constitute related cost to Revenue.

- For example, assuming an Accounting Firm won a contract of service worth N1m and the only cost incurable is the purchase of a Laptop worth, say N200,000. Many have justified the quoted paragraphs (in this case *IAS 18 p. 20d* since it is a service contract) as reason for expensing the laptop that otherwise falls within the scope other Standards (in this case IAS 16). IFRS 15

has resolved the potential for ambiguous interpretation in IFRS 15 p. 95, 96 by requiring an initial check of whether costs associated with revenues falls within the scope of another Standard (e.g. IAS 2, IAS 16, IAS 38), if so, these Standards prevail over IFRS 15 as far as the costs are concerned.

- Significant financing components: In instances where transaction price exceeds the cash price of a merchandize solely due to the potential for deferred payment, IAS 18 p. 11 requires that the entity recognizes revenue in the amount of the cash selling price whilst the difference between the cash price and the transaction price qualifies as finance income, treated separately from revenue in the income statements.

- Many found it difficult applying this provision of the Standard to short term delays in receiving cash e.g. between 6 – 8months delay; the question many asked is how many months of delays qualify as settlement on deferred terms?

- IFRS 15 p. 63 resolved this with a provision to ignore the existence of significant financing component if the deferred period is 12months or less.

- Further, it would appear that IAS 18 p. 11 only envisaged suppliers' credit (i.e. customers' delays resulting in premium payment).

- In practice, either party could enjoy credit since customers could also pay less by paying in advance. Again, IFRS 15 takes cognizance of this in paragraph 60.