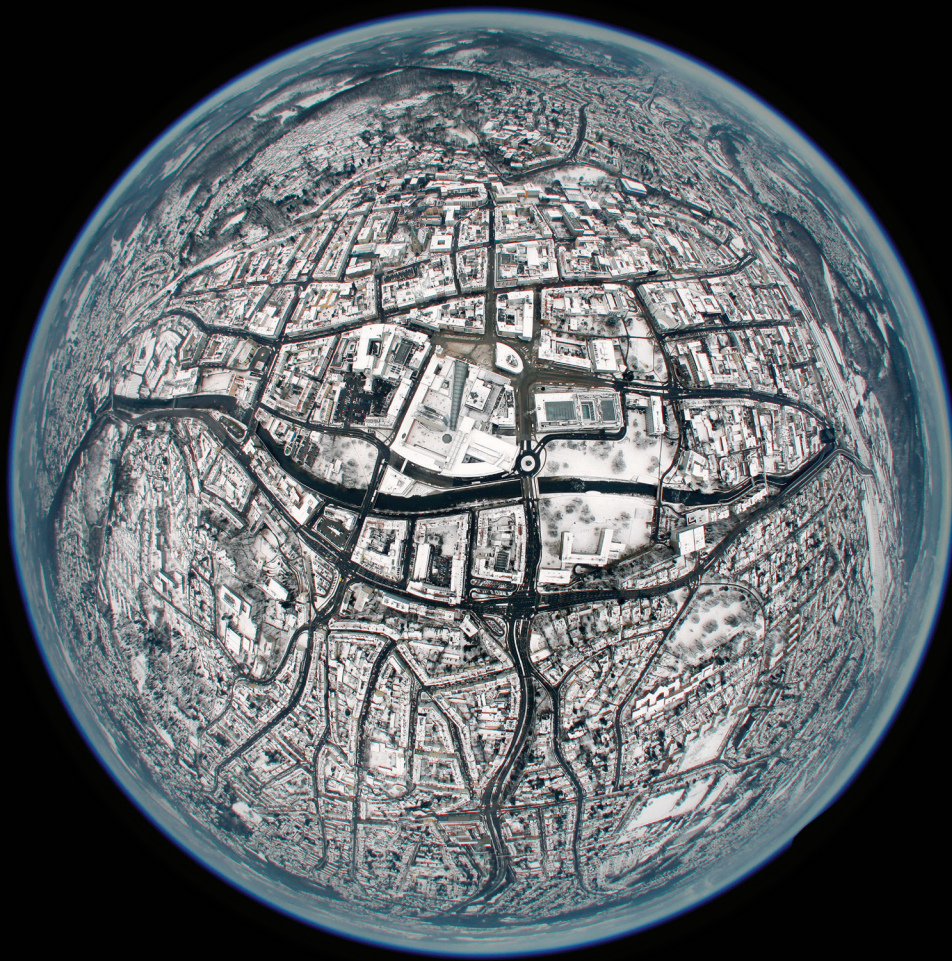


**Deloitte.**



**The Navigator**

AASB 15 Revenue from  
contract with customers



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# About this guide

AASB 15 Revenue from Contracts with Customers ('AASB 15' or 'the standard' or 'the new standard') was issued by the Australian Accounting Standards Board ('AASB') in December 2014 based on IFRS 15 Revenue from contracts with customers ('IFRS 15') issued by the International Accounting Standards Board ('IASB') in May 2014.

A number of implementation issues have emerged since the standard was published that are subject to ongoing discussion at the Joint Transition Resource Group ('TRG'), a panel formed by the IASB and the Financial Accounting Standards Board ('FASB'). As a result of these discussions, it is expected that additional guidance will be issued to provide clarity on certain parts of the standard.

Application of AASB 15 is expected to have varying levels of impact across organisations and industries. In some circumstances, the degree of complexity, judgement and disclosure requirements will require substantial changes to an organisation's financial reporting systems and processes, while possibly resulting in the disclosure of commercially sensitive information.

For successful implementation, it is critical that organisations do not focus only on apparent differences between current accounting standards and AASB 15. The full impact of AASB 15 can only be understood when contracts are assessed using the new guidance in its entirety. Early assessment and planning will ensure implementation risks and exposures are appropriately managed.

This publication sets out an overview of AASB 15. It summarises the key concepts underpinning the framework for recognition and measurement of revenue and identifies areas where significant judgement may be required. This guide is neither intended to be exhaustive nor provide solutions to all the issues relating to AASB 15, but rather aims to highlight the key requirements under the new standard and provide reference to the paragraphs and illustrative examples contained within AASB 15.

We hope you will find this guide helpful and encourage you to consult where appropriate should you find yourself facing issues when interpreting and implementing AASB 15. See [www.iasplus.com](http://www.iasplus.com) for further insights into IFRS 15.

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# Overview

## A new accounting standard on revenue recognition:

- AASB 15 provides a new framework for revenue recognition (when to recognise revenue) and measurement (at what amount) following a five-step approach. The new standard replaces the existing accounting literature for revenue recognition which is currently spread across various standards and Interpretations, both under IFRS and US GAAP
- The mandatory effective date is for reporting periods beginning on or after 1 January 2018 with early adoption permitted. For Australian entities with June year-ends, AASB 15 will be effective

from 1 July 2018. It is noted that, at the time of this publication, the IASB and AASB have issued an Exposure Draft seeking comments in respect of the deferral of the effective date of IFRS15/ AASB 15 to annual reporting periods commencing on or after 1 January 2018, with early adoption still permitted

- AASB 15 will apply to contracts of not-for-profit ('NFP') entities that are exchange transactions. AASB 1004 Contributions will continue to apply to non-exchange transactions until the income from transactions of not-for-profit entities project is completed by the AASB. An exposure draft on this project was issued in May 2015.

## Implementation of AASB 15: where to start?

The core principles of the revenue model as described in the new Standard are as follows:

When is revenue recognised?

When or as the entity satisfies a performance obligation by transferring a good or service to a customer.

How much revenue is recognised?

The amount that represents the consideration to which the entity expects to be entitled.

The core principles are supported by the following five steps and disclosure requirements, as discussed in this document:



**Step 1:**  
Identify the contract(s) with the customer  
[AASB 15.9–21]



**Step 2:**  
Identify separate performance obligations in the contract  
[AASB 15.22–30]



**Step 3:**  
Determine the transaction price  
[AASB 15.47–72; 87–90]



**Step 4:**  
Allocate the transaction price to separate performance obligations  
[AASB 15.73–86]



**Step 5:**  
Recognise revenue when(or as) each performance obligation is satisfied  
[AASB 15.31–46]



**Contract Costs**  
[AASB 15.91–104]



**Disclosures**  
[AASB 15.110–129]

**AASB 15 is not merely a financial reporting issue:**

The requirements of the standard are such that they may have a widespread impact on an organisation. Apart from preparing the market and educating analysts and shareholders on the impact of the new standard, entities will need to consider wider implications. Amongst others, these may include:



**Management and information systems**



**Commercial**



**Financial compliance**



**System changes**

Assessing data capture and reporting capabilities to identify gaps in the current systems and upgrading IT systems, internal processes and controls where required.



**Contract management**

Factoring the impact of AASB 15 into the entity's assessment of new contracts that are currently being negotiated to manage exposure.



**Bank loans**

Assessing the likely impact of AASB 15 on the entity's revenue and profit profile when entering into new banking facilities and negotiating covenants.



**Forecasts**

Factoring the impact of the new standard on both the timing and amount of revenue recognised into any profit forecasts that the entity prepares.



**Employees**

Understanding remuneration schemes, the impact of the standard on the timing of targets being achieved and the likelihood of targets being met. This may prompt a revision to KPIs. Entities need to identify appropriate communications and training needs of employees to maintain employee engagement and effectively project manage the implementation of AASB 15.



**Taxation**

Assessing the potential impact on taxable income and deferred taxes to identify changes to the profile of tax cash payments, if any.

- Revenue recognition under AASB 15 will primarily be based on a set of principles that will require the determination of numerous estimates and extensive use of judgement, while certain parts of the standard are rules based and prescriptive in nature. In some cases irreversible elections will need to be made
- AASB 15 introduces new complexities both for the timing of revenue recognition and the quantum of revenue to be recorded. For a complete and effective implementation, entities will need to embrace the new model in this standard rather than assessing the changes from the existing guidance only. The impact of AASB 15 can only be fully understood when material contracts and transactions are assessed using the new guidance in its entirety
- There are significant additional disclosure requirements. This will have a pervasive impact and entities will need to assess whether appropriate systems and processes are in place to collate the required information and to assess where disclosures may contain sensitive information
- Entities will need to maintain dual systems and accounting records to comply with the transition requirements of the standard
- Early planning is critical to ensure implementation risks and exposures are managed.



### Plan the implementation process:

The extent of impact will differ from entity to entity. Early assessment and planning will ensure implementation risks and exposures are appropriately managed. Some of the key activities to be considered in developing a tailored project plan are set out below:



#### Assess the impact

- Establish project management team
- Identify stakeholders and assess their needs
- Evaluate significant revenue streams and their components
- Identify, evaluate and summarise key contracts
- Capture and define key accounting issues and new policy requirements
- Determine additional disclosure needs
- Analyse data capture requirements, capabilities and identify gaps
- Assess other potential process and business impacts, e.g. KPI, bonus structures, forecasting, loan covenants, etc.



#### Design the solution

- Draft the implementation plan
- Design and develop accounting, systems and process solutions
- Pilot testing of solution design.



#### Implement the plan

- Deployment of accounting systems and process solutions across organisation
- Training of employees.



#### Review the results

- Post implementation review, verification and monitoring.



## Step 1: Identify the contract with a customer

AASB 15 only applies where a contract exists and where that contract is with a customer [AASB 15.6].

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.

The new standard specifically scopes out lease contracts, financial instruments, insurance contracts and non-monetary exchanges between entities in the same trade [AASB 15.5]. However the sale of certain non-financial assets that are not an output of an entity's ordinary activities, e.g. sale or transfer of property, plant and equipment, will be scoped into this standard.

Although a gain or loss on this type of sale generally does not meet the definition of revenue, an entity should apply the guidance in AASB 15 relating to the transfer of control and measurement of the transaction price, including the constraint on variable consideration, to evaluate the timing and amount of the gain or loss to be recognised.

The standard is to be applied and assessment made on a contract by contract basis, except where an entity elects and meets the criteria to apply a 'portfolio approach' [AASB 15.4].

The standard may be applied on a portfolio basis if (a) it is applied to a group of contracts (or performance obligations) with 'similar characteristics' and (b) the entity 'reasonably expects' that the effects on financial statements are not 'materially different' to the effects of applying the standard on a contract by contract basis.

Demonstrating that there is no material difference in applying the standard on a portfolio basis vis-a-vis on a contract by contract basis can be very complex.

Once within scope, the requirements relating to modifications of contracts and contract combination must be considered.

### **In-scope contracts:**

#### **When does a contract exist?**

An entity should account for a contract with a customer that is in the scope of AASB 15 when all of the following criteria are met [AASB 15.9]:

A contract is an agreement between two or more parties that creates enforceable rights and obligations.

*Has the transaction been approved and have the parties committed to their respective obligations?*

*Can the entity identify each party's rights regarding goods/services to be transferred?*

*Can the entity identify the payment terms for the goods/services to be transferred?*

*Is there commercial substance?*

*Is the collection of consideration probable based on the customer's ability and intention to pay?*



**Further considerations:**

It is important to consider the following additional guidance when making this assessment:

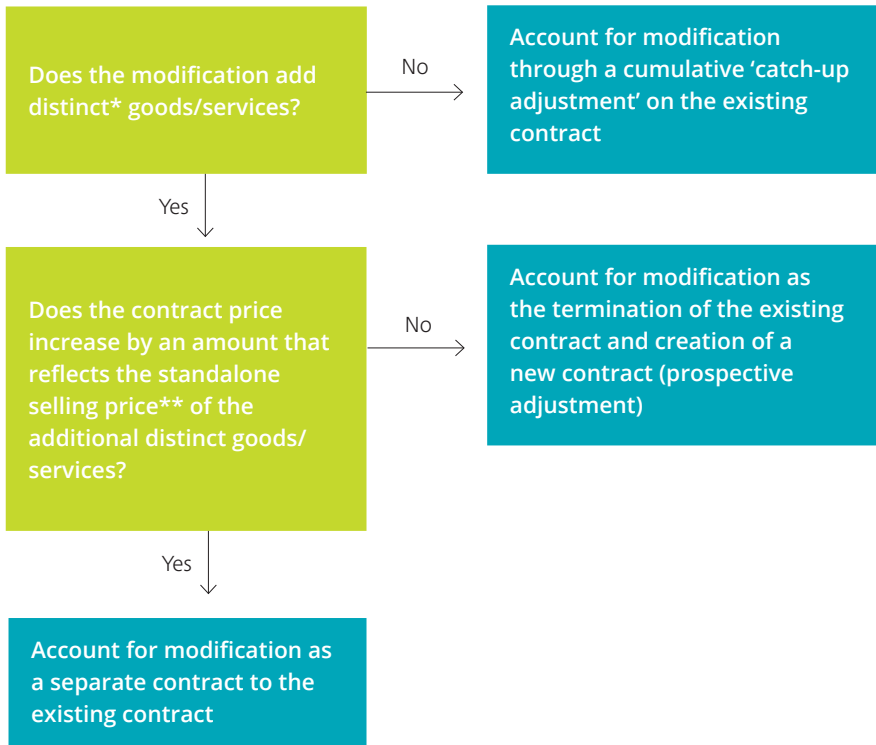
- **Contract approvals:** Agreements can be verbal, written or implied. The focus is on whether there are 'legally enforceable rights and obligations' [AASB 15.10]
- **Contract combination:** Contracts entered into at (or near) the same time with the same (or related) customer should be combined if any one of the following criteria is met:
  - Contracts have a single commercial objective
  - Consideration or performance under the contracts is interdependent
  - Promised goods or services are a single performance obligation [AASB 15.15–17]

- **Contract does not exist:** If the criteria for determining whether a contract exists are not met, the entity should continue to assess the contract to determine whether those criteria are subsequently met [AASB 15.14].

Any consideration received in the absence of a contract is recorded as a liability until (a) all the obligations are fulfilled and the amount is non-refundable or (b) the agreement is terminated and the amount received is non-refundable [AASB 15.15–16].

**Modifications:**

A modification is a change to an existing contract which changes the scope of the contract and/or the price of the contract. A contract modification exists when the parties to the contract have approved the modification either in writing, orally or based on their customary business practices [AASB 15.18–19].



\* The concept of 'distinct' is discussed in Step 2 Identify the performance obligation.

\*\* The concept of 'standalone selling price' is discussed in Step 4 Allocate the transaction price.



### To consider:

- Is there a contract?
- Is the contract scoped out of the standard?
- Will the Standard be applied to a portfolio of contracts or on a contract-by-contract basis?
- Are there any side agreements/multiple agreements which need assessment for contract combination?
- Have any of the contractual terms changed?
- Do factors exist which can lead to a modified contract, e.g. change in scope and/or price?

- In some circumstances, the determination of whether a contract falls within the scope of AASB 15 or another standard requires significant judgement. Entities will need to factor in the possibility that a contract may only be partially in scope of AASB 15; e.g. a contract for the lease of equipment and the provision of services may need to be assessed separately under the accounting standard for leases and this standard
- When applying the standard to account for the gain or loss arising on the sale of non-financial assets, e.g. the sale of buildings, an entity needs to take note of any repurchase clauses included in the agreement. If any such clause exists, entities will be required to apply the AASB 15 guidance relating to repurchase agreements, which is discussed further in Step 5
- An entity needs to exercise significant judgement to evaluate whether contracts have 'similar characteristics' and to establish a 'reasonable expectation' that the effects of using a portfolio approach would not differ materially from those of applying the guidance at a contract or performance obligation level. There is a need for documented support of such assessment
- An entity should first determine whether it expects to accept a lower amount of consideration from the customer than what the customer is obligated to pay, i.e. offer a price concession to the customer, before assessing whether collectability is 'probable'. Collectability will then be based on the lower amount of consideration
- Legal enforceability depends on the interpretation of the law and could vary across legal jurisdictions
- Robust systems are required to identify and significant judgement is required to ascertain how to account for contract modifications
- When accounting for contract modifications where a scope change has been agreed without a corresponding approval of price, entities need to consider the guidance on estimating variable consideration. Consideration should be given to all facts and circumstances, including, but not limited to, prior experience with similar modifications, in determining whether the price change will be approved by the customer.



### AASB 15 reference:

AASB 15.5–21; Appendix A

#### Illustrative Examples:

**Example 1** – Collectability of the consideration

**Example 2** – Consideration is not the stated price – implicit price concession

**Example 3** – Implicit price concession

**Example 4** – Reassessing the criteria

for identifying a contract

**Example 5** – Modification of a contract for goods

**Example 6** – Change in the transaction price after a contract modification

**Example 7** – Modification of a services contract

**Example 8** – Modification resulting in a cumulative catch-up adjustment to revenue

**Example 9** – Unapproved change in scope and price

**Basis for Conclusions:** BC28–BC83



## Step 2: Identify the performance obligation

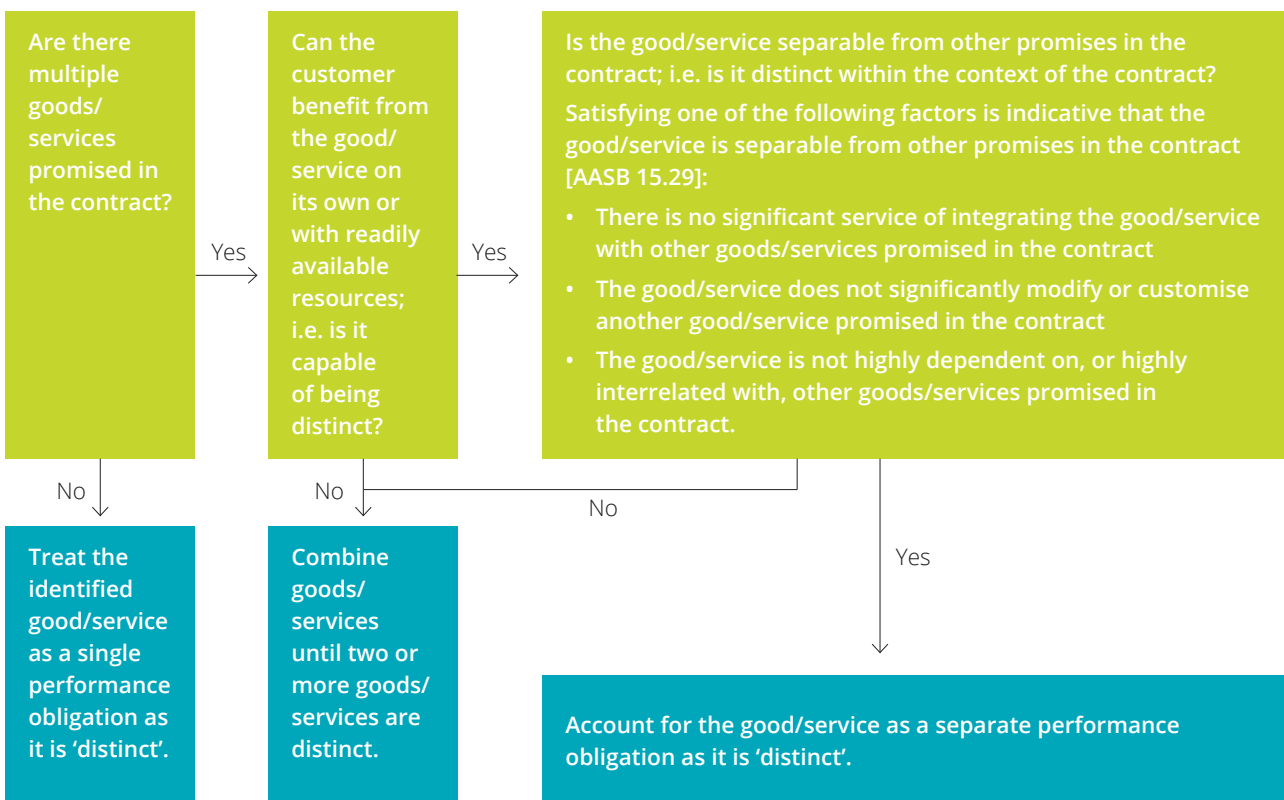
A performance obligation is the level at which an entity needs to ascertain the timing and quantum of revenue to be recognised.

### How is a performance obligation identified?

A performance obligation can be either (a) a good/service that is distinct or (b) a series of distinct goods/services that are substantially the same and have the same pattern of transfer to the customer [AASB 15.22]. Identification and determination of performance obligations takes place at contract inception and will not change unless there is a contract modification.

### Criteria for a good/service being 'distinct':

Entities will need to identify all promised goods/services in the contract and assess whether these goods/services are distinct on their own or in combination with other goods/services. The following guidance should be used when making this assessment [AASB 15.26–30]:



**Example of goods/services that are not distinct**

An entity (contractor) enters into a contract to build a hospital for a customer. The entity is responsible for the overall management of the project and identifies various goods/services to be provided, including engineering, site clearance, foundation, procurement, construction of the structure, piping and wiring, installation of equipment and finishing.

The promised goods/services are capable of being distinct since the customer can benefit from them either on their own or together with other readily available resources. This is evidenced by the fact that the entity, or competitors of the entity, regularly sells many of these goods/services separately to other customers.

However, the goods/services are not distinct within the context of the contract as the entity's promise to transfer individual goods/services in the contract are not separately identifiable from other promises in the contract. This is evidenced by the fact that the entity provides a significant service of integrating the goods/services (the inputs) into the hospital (the combined output) for which the customer has contracted.

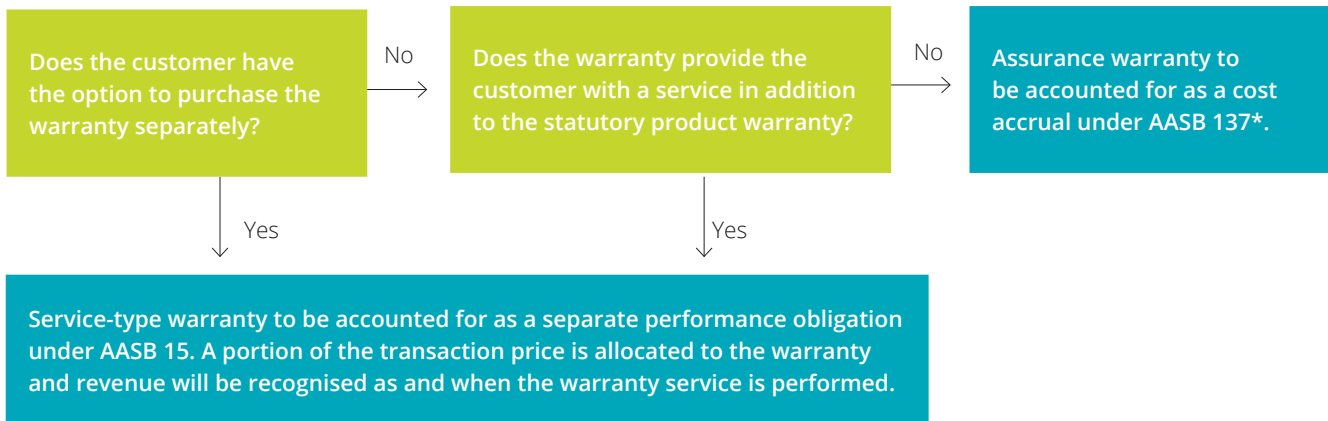
Since both criteria are not met, the goods/services are not distinct. The entity will account for all of the goods/services in the contract as a single performance obligation. A careful assessment of specific facts and circumstances will be required to determine the appropriate accounting treatment in these scenarios.

**Further considerations:**

**Warranties:**

Entities often provide customers with a warranty in connection with the sale of goods/services, which can take many different forms varying across industries and jurisdictions, whether explicitly contained within the contract or implicit as a result of customary business practice or legal requirements [AASB15.B28].

An entity should assess the nature of the warranty to determine the appropriate accounting [AASB 15.B29 – B33].



\* AASB 137 Provisions, Contingent Liabilities and Contingent Assets.

**Example**

A television is sold to a customer with a statutory warranty period of two years and allowing the customer an option to purchase an additional two year warranty. The statutory warranty will be accounted for as a cost accrual under AASB 137 while the additional warranty will be accounted for as a separate performance obligation under AASB 15.

**Option to acquire additional goods/services:**

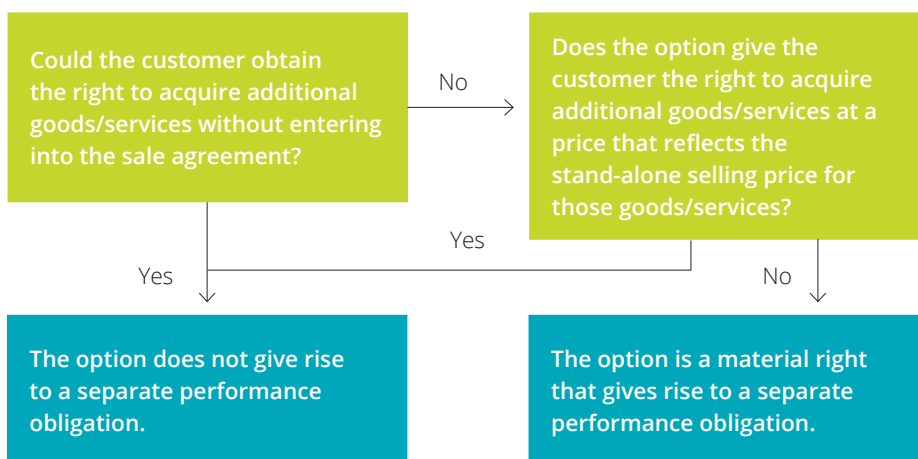
Contracts with customers may contain rights that provide the customer with an option to purchase additional goods/services for free or at a discount, e.g. sales incentives, customer award credits or points, contract renewal options, and discounts on future goods/services [AASB 15.B39]. An entity is required to account for the customer option to acquire additional goods/services as a separate performance obligation if the option provides the customer with a material right [AASB 15.B40].

**Set-up activities:**

Activities that an entity undertakes to fulfil a contract that do not transfer goods/services to the customer, e.g. administrative tasks to set up a contract, are not performance obligations. In some circumstances, a careful analysis will be required to determine if set-up activities have transferred a distinct good/service to the customer [AASB 15.25]. Entities may be able to capitalise costs incurred on these set-up activities if certain criteria are met. For further discussion on capitalisation of contract costs, refer to the section on Contract costs in this guide.

**Implicit promises in a contract:**

A contract with a customer may contain promises which are implied by the entity's customary business practices, published policies or statements, e.g. an entity advertises to provide free maintenance services in a marketing campaign. If at the time of entering into the contract, such promises create a valid expectation of the customer that additional goods/services will be delivered and the goods/services are 'distinct', then the entity should not recognise revenue until such goods/services are delivered [AASB 15.24].





### To consider:

- Are there multiple deliverables in the contract?
- For contracts with several deliverables, can the customer benefit from any of the deliverables independently or using a readily available resource?
- What happens if the entity never sells the goods/services separately?
- Does the entity provide an integrated good/service?
- Is there is a significant modification or customisation involved for the good/service to be delivered?
- Would a customer buy one good/service without the other in the bundle?
- Does the activity performed by the entity result in the transfer of a good/service to the customer?

- Assessment of performance obligations must be made at contract inception
- Significant judgement is required when assessing the 'distinct' criteria for a promised good/service, especially in relation to determining whether the good/service is 'distinct within the context of the contract'. The assessment of when to separately identify and account for a performance obligation in accordance with this guidance has posed significant challenges to date and has been subject to debate at the Joint Transition Resource Group. The IASB may issue additional guidance to clarify this criterion
- Only those activities performed by an entity that result in the transfer of a good or service to a customer can give rise to a separate performance obligation. In some circumstances a careful analysis of activities is required to determine whether a separate performance obligation exists or whether the activity is part of delivering a performance obligation, e.g. set up activities, mobilisation of resources
- An entity needs to carefully assess whether there are any implied promises in the contract as implied promises can lead to revenue deferral until the implied promise to transfer the good/service is met.



### AASB 15 reference:

AASB 15.22–30; B28–B33; B39–B43; B52–B56

### Illustrative Examples:

**Example 10** – Goods and services are not distinct

**Example 11** – Determining whether goods or services are distinct

**Example 12** – Explicit and implicit promises in a contract

**Basis for Conclusions:** BC84–BC116



## Step 3: Determine the transaction price

As and when a performance obligation is satisfied an entity should recognise revenue to the extent of the transaction price allocated to that performance obligation taking into account the impact of constraints arising from variable consideration [AASB 15.46].

The transaction price is the amount of consideration to which the entity is expected to be entitled in exchange for transferring a promised good/service to a customer.

The transaction price is estimated by the entity at contract inception. The estimate is updated at each reporting date for any changes in circumstances which will include reassessment of any variable component identified and relevant modifications to the contract.

### What impacts the amount of revenue?

The nature, timing and amount of consideration promised by a customer affects the estimate of the transaction price. When determining the transaction price an entity should consider all of the following:

### Variable consideration:

Variable consideration includes discounts, rebates, refunds, credits, incentives, performance bonuses/penalties, contingencies, price concessions, or similar items. Variability in consideration can arise from either the amount being:

- Variable as explicitly stated in the contract or arising from customary business practice of the entity or
- Fixed but its receipt is contingent on the occurrence of a future event.

An entity needs to estimate the amount of variable consideration to which it will be entitled, taking into account the recognition threshold described below [AASB 15.50, 56]. The recognition threshold limits rather than precludes revenue recognition.

### Recognition threshold

Variable consideration is included in the transaction price to the extent it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur when the uncertainty is subsequently resolved.

Conditions which enhance the risk of cumulative revenue recognised being reversed include:

- Amount is highly susceptible to factors outside the entity's influence
- Uncertainty is not expected to be resolved for a long period of time
- The entity has limited experience with similar contracts or does not have adequate data to predict value
- The entity has a practice of offering price concessions or changing payment terms
- The contract has a large number and broad range of possible price variations.

Variable consideration is measured using one of the following methods:

- Expected value – sum of probability-weighted amounts in a range of possible outcomes
- Most likely amount – single most likely amount, if outcome is binary in nature.

### Significant financing component:

An entity is required to consider all facts and circumstances to ascertain if a contract contains a significant financing component. If a significant financing component exists consideration is allocated between revenue and interest expense or interest income depending on whether the entity has received financing from its customer (advance payments) or provided financing to its customer (deferred payments) [AASB 15.61]. As a practical expedient, if the time gap between delivery of goods/services and payment is one year or less, an entity does not need to adjust the consideration for the effects of financing [AASB 15.63].

In determining whether a significant financing component exists, consider:

- The difference in the amount of consideration and the cash selling price – a significant difference indicates the existence of an implicit financing arrangement
- The combined effect of:
  - Expected time lag between delivery of goods/services and payment. The longer the time gap, the greater the possibility that a financing component exists
  - Prevailing interest rates in the market.

If a significant financing component exists, the entity should measure the interest income or expense using a discount rate that reflects the rate that would be used in a separate financing transaction between the entity and its customer. This rate should reflect the credit risk of the party obtaining financing in the arrangement which could be the entity (if receiving advance payments) or the customer (if making deferred payments).

A contract with a customer will not have a significant financing component if any of the following factors exist:

- The amount is paid by the customer in advance but the timing of receipt of goods/services is at the customer's discretion
- A substantial amount of consideration is variable and based on occurrence of a future event
- The timing difference in delivery of goods/services and payment occurs for reasons other than financing, e.g. the customer retains payments (retentions) as a protective mechanism for the performance of an appropriate quality of work by the entity.

### Non-cash consideration:

Any non-cash consideration received from a customer needs to be included when determining the transaction price and should be measured at its fair value. If the form of consideration, e.g. shares of the customer, makes its fair value variable, then it is reflected in the assessment of the transaction price and is not subject to the constraint on variable consideration [AASB 15.66–69].

### Consideration payable to customer:

Consideration paid to a customer is accounted for as a reduction of revenue unless the payment relates to the customer providing distinct goods/services to the entity in which case it is recorded as a separate transaction with the customer [AASB 15.70–72].

### Example

If the customer provides advertising services for the entity's products and is paid fair value by the entity, then the amount paid to the customer will be viewed as a cost of advertising for the entity; while an amount paid to the customer to place the products in a favourable location ('slotting') in the retail store may not result in a separate service being provided by the customer to the entity, thus resulting in the entity recording the amount as a reduction of revenue.

A careful assessment of specific facts and circumstances will be required to determine the appropriate accounting treatment in these scenarios.

### Right of return:

Many entities offer their customers a right to return purchased products. This right of return can take different forms, e.g. entitling a customer to a full or partial refund of the amount paid, a credit against the value of previous or future purchases, or an exchange of one product for another [AASB 15.B20]. Understanding the rights and obligations of both parties in an arrangement when return rights exist is critical to determining the accounting [AASB 15.B21].

### Example

An entity sells 100 units for \$50 each. Each unit has a cost of \$10 and the entity expects that 15 units will be returned. As the entity expects to refund the sales price when the customer returns the goods, the following should be recognised by the entity:

- Revenue, but only to the extent of the entity's expectation that the customer will not return the goods; i.e. 85 units at \$50 each
- A refund liability for the portion expected to be returned, i.e. 15 units at \$50 each
- An asset with a corresponding adjustment to cost of sales for the right to recover products from customers on settling the refund liability, i.e. 15 units at \$10 each.





### To consider:

- Does the entity offer variable pricing to its customers, either through customary business practice or as per the contract; e.g. discounts, rebates, performance bonuses, refunds, penalties?
- Are there any contingent events, the occurrence of which will trigger consideration from the customer?
- Does the entity have adequate data to estimate the variable consideration?
- Have there been any changes in the transaction price since inception of the contract?
- Is there a time lag between collection of money and delivery of goods/provision of services?
- Does the entity have any 'buy now, pay later' offers?
- Are there any provisions for the customer to pay by a means other than cash or credit, e.g. shares of the customer or other goods/services provided by the customer?
- Does the entity pay any amount to the customer? If so, what is the reason for such a payment?

- When an entity is considering whether a contract contains a significant financing component or is assessing the highly probable threshold for recognition of variable consideration, it needs to exercise significant judgement which will require additional documentation and disclosure
- Entities will need to assess different types of variable consideration in their business
- In some cases the entity may be subject to liquidated damages or penalties that may result in the entity not recognising revenue or recognising a net expense
- Entities need to be aware of the different thresholds to be applied for assessing 'collectability' in Step 1 and the 'variable consideration constraint' in Step 3. Assessment of 'collectability' is based on a 'probability' threshold while constraining the amount of variable consideration to be recognised is based on a 'highly probable of no significant reversal' threshold. Once revenue has been recognised any bad debt provision is assessed on the gross amount of revenue recognised and the bad debt is recognised as an expense
- If an entity receives upfront payments or cash advances from a customer it will need to assess the existence of an implicit financing transaction, in which case the amount of revenue recognised will be adjusted with a corresponding interest expense recognised in the income statement
- There are now specific requirements in the standard in relation to the measurement of non-cash consideration and how to account for any amounts that an entity may pay to its customers
- If the contract contains a significant financing component, the discount rate used for measuring the interest income or expense is not the implicit rate in the contract, rather it is the market interest rate reflecting the credit risk of the party obtaining the finance. Accordingly if multiple customers make deferred payments, an entity may recognise different revenue amounts for contracts with similar terms if the credit profiles of the customers differ.



### AASB 15 reference:

AASB 15.46-72; B20-B27

#### Illustrative Examples:

- Example 20**–Penalty gives rise to variable consideration
- Example 21**–Estimating variable consideration
- Example 22**–Right of return
- Example 23**–Price concessions

**Example 24**–Volume discount incentive

**Example 25**–Management fees subject to the constraint

**Example 12** – Explicit and implicit promises in a contract

**Example 26** – Significant financing component and right of return

**Example 27** – Withheld payments on a long-term contract

**Example 28** – Determining the discount rate

**Example 29** – Advance payment and assessment of the discount rate

**Example 30** – Advance payment

**Example 31**– Entitlement to

non-cash consideration

**Example 32** – Consideration payable to a customer

**Basis for Conclusions:**

BC181–BC265



## Step 4: Allocate the transaction price

After determining the transaction price at Step 3, Step 4 specifies how an entity should allocate that transaction price between the various performance obligations identified in Step 2. This is particularly relevant when the timing of revenue recognition varies for each of the performance obligations.

### What is the basis of allocation?

#### Stand-alone selling price:

The transaction price should be allocated to each performance obligation based on the relative stand-alone selling prices of the goods and services being provided to the customer [AASB 15.76].

The best evidence of a stand-alone selling price is the price the entity charges for each good/service when selling them separately to similar customers and under similar circumstances [AASB 15.77].

At inception of the contract the stand-alone selling price should be determined together with the allocation of the transaction price to various performance obligations. The basis of the allocation cannot change at a later date [AASB 15.88].

In some circumstances stand-alone selling prices are not observable and therefore an entity may need to estimate the stand-alone selling price of a performance obligation using one of the following approaches [AASB 15.79]:

- 1. Adjusted market assessment approach:** based on the current market, estimate the price that customers would be willing to pay for the good/service
- 2. Expected cost plus margin approach:** determine the expected cost to satisfy the performance obligation and add an appropriate margin
- 3. Residual approach:** deduct all stand-alone selling prices of the other goods/services from the total transaction price and allocate the residual to the remaining good/service.

The existence of variable consideration [AASB 15.84–86], discounts [AASB 15.81–83] or changes to the transaction price after inception of the contract [AASB 15.87–90] will require a careful analysis to determine whether any of these items should be allocated to a specific performance obligation or on a pro-rata basis across multiple performance obligations.

### Example

Entity X enters a contract with a customer to sell goods/services A, B and C for \$100.



The stand-alone selling prices are estimated as follows:

#### Item A –

Directly observable price \$50

#### Item B –

Adjusted market assessment approach \$25

#### Item C –

Expected cost + margin approach \$75

The customer receives a discount for purchasing the bundle of goods and services, because the sum of the stand-alone selling prices (\$150) exceeds the promised consideration (\$100).

The discount is allocated proportionally to all performance obligations unless there is observable evidence that the entire discount relates to one or more specific performance obligation(s) in the contract.

#### Allocation of transaction price \$100:

$$A \$33 = \$50 / \$150 \times \$100$$

$$B \$17 = \$25 / \$150 \times \$100$$

$$C \$50 = \$75 / \$150 \times \$100$$



### To consider:

- Does the entity regularly offer bundled pricing on products it sells separately?
- Does the entity provide discounts on bundled goods/services which need to be allocated?
- Has the entity offered a discount for only one good/service within a bundle?
- Is there variable consideration which requires allocation?
- Are stand-alone selling prices observable?
- Is there a need to allocate changes in the transaction price to individual performance obligations?

- AASB 15 contains reasonably prescriptive guidance on recognition and measurement of revenue arising from contracts containing bundled goods/ services while the existing accounting standards contain very little in terms of this requirement. Accordingly this could be an area of significant change for some entities and entities will need to consider whether their existing systems and processes are capable of allocating the transaction price in accordance with the new standard
- The transaction price must be allocated to goods/services irrespective of whether an observable price exists. There is no exception available due to a 'lack of reliable information
- The relative stand-alone selling price of each performance obligation is determined at contract inception and is not reallocated to reflect subsequent changes in stand-alone selling prices.



### AASB 15 reference:

AASB 15: 73–90

### Illustrative Examples:

**Example 33** – Allocation methodology

**Example 34** – Allocating a discount

**Example 35** – Allocation of variable consideration

**Basis for Conclusions:** BC266–286



# Step 5: Recognise revenue when (or as) the performance obligation is satisfied

The final step is to determine, for each performance obligation, when revenue should be recognised.

### When to recognise revenue?

An entity recognises revenue as and when each performance obligation is satisfied by transferring control of a promised good/service to the customer [AASB 15.31].

Control is the ability to direct the use of and obtain substantially all of the benefits from the goods/services and/or the ability to prevent others from obtaining benefits from the use of the goods.

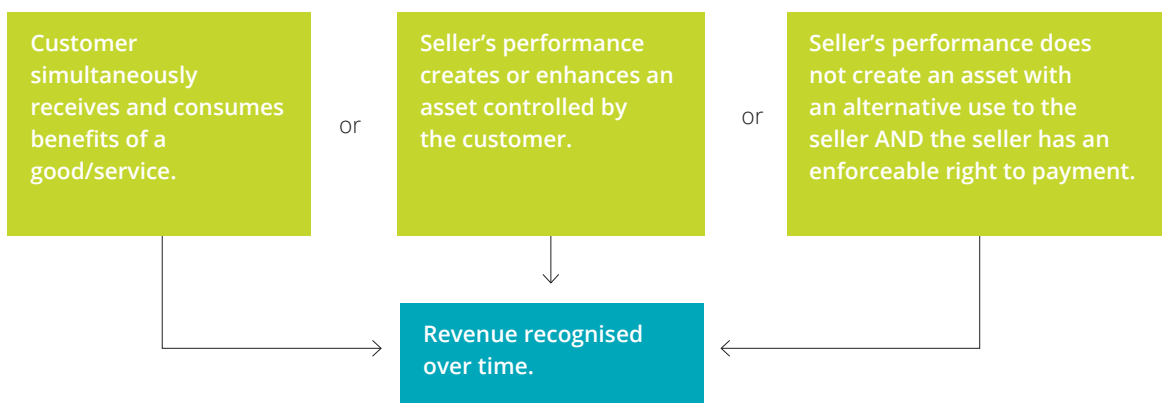
### Satisfaction of performance obligations:

At contract inception an entity needs to determine whether control of a good/service transfers to the customer over time or at a point in time using the criteria below [AASB 15.35–37]. This determination is not expected to change over the life of the contract. For all other performance obligations, revenue is recognised at a point in time.

### Measurement of progress:

- For revenue recognised over time, an entity needs to measure the progress towards complete satisfaction of the performance obligation with the objective of recognising revenue that depicts the entity's performance in transferring control of the goods/services to the customer [AASB 15.39]

- An entity's selection of an input method (e.g. percentage cost completion method) or an output method (e.g. assessing value transferred) for this purpose is not an accounting policy choice, rather the method selected must be able to best depict the pattern of transfer of goods/services to the customer [AASB 15.41–45].



For performance obligations satisfied at a point in time, an entity is required to assess when control has been transferred to the customer by considering the following indicators [AASB 15.38].



Customer has legal title



Customer has physical possession



Customer has significant risks and rewards of ownership



Customer has accepted the goods/services



Entity has present right to payment

Not all of the above indicators need to be present for an entity to conclude that it has transferred control to a customer.

When evaluating whether a customer has obtained control of the goods/services, an entity should consider the existence of any repurchase agreements [AASB 15.34].

### Application guidance in specific circumstances

#### Repurchase agreements:

- ▶ Repurchase rights are an obligation or right to repurchase a good after it is sold to a customer, which can take the form of a put option, a call option or a forward contract. The existence of these clauses can have a significant impact on the accounting for the contract. Depending on the facts and circumstances, the arrangement may be recorded as a sale, a lease contract or as a financing agreement [AASB 15.B64–B76].

#### Customers' unexercised contractual rights:

- ▶ When an entity receives a non-refundable prepayment from the customer, e.g. sale of gift cards, gift certificates or lay-by sales, the customer has an unexercised right to receive goods/services in the future, which some customers may not use (typically termed as 'breakage'). An entity is required to consider whether or not the customer will eventually exercise their rights which will impact the entity's pattern of revenue recognition [AASB 15.B44–B47].

#### Consignment arrangements, bill-and-hold arrangements:

- ▶ An entity must consider the existence of these arrangements when determining the point in time that it transfers control to the customer as this could impact the timing of revenue recognition [AASB 15.B77–B82].

#### Non-refundable upfront fees:

- ▶ If contracts include non-refundable upfront fees from customers, revenue recognition should be delayed if the fees relate to future goods/services to be transferred to the customer [AASB 15.B48–B51].

#### License:

- ▶ If the licence of intellectual property is considered a separate performance obligation, an entity is required to assess the nature of the licence to determine whether to recognise revenue at a point in time or over time [AASB 15.B52–B62]. An entity should recognise a sales-based or usage-based royalty only on the occurrence of the subsequent sale or usage [AASB 15.B63].



**To consider:**

- Is the entity selling a customised good?
- What are the payment terms?  
Does it create an enforceable right for the entity?
- Are there clauses in the agreement that are in the nature of forward sale or purchase, put and/or call options?
- When does the customer gain control over the good/service?
- Is usage of the percentage of completion method still appropriate to measure revenue?
- Does the entity receive any non-refundable upfront fees?  
What rights does the customer have as a result of the upfront fee?
- Does the entity have licensing arrangements?

- Revenue recognition over time is not limited to only service arrangements. Depending on the terms of the agreement revenue may be recognised over time when the entity constructs customised goods or complex assets for the customer depending on whether the entity has payment rights over the period
- Not all the indicators for transfer of control need to be present for an entity to conclude that it has transferred control to its customer. Similarly the standard does not provide any guidance on whether more weight is to be placed on one indicator over the others. Significant judgment is required to determine if control has been transferred
- For any licensing arrangements an entity needs to exercise significant judgement when determining whether the licence is a separate performance obligation within the contract and the appropriate timing of revenue recognition from such licences. This is an area that has undergone significant debate by the IASB and is still subject to discussion at the Joint Transition Resource Group. The IASB is expected to issue additional guidance on license arrangements
- The timing of revenue recognition will be subject to significant judgement, especially when there are repurchase clauses (puts, calls and/or forwards) within an agreement or when the entity receives non-refundable upfront fees.



**AASB 15 reference:**

AASB 15.31-38; B2-B19; B44-B51; B57-B86

**Illustrative Examples:**

- Example 13** – Customer simultaneously receives and consumes the benefits – Services
- Example 14** – Assessing alternative use and right to payment – Services
- Example 15** – Asset has no alternative use to the entity – Construction
- Example 16** – Enforceable right to payment for performance completed to date – Construction

- Example 17** – Assessing whether a performance obligation is satisfied at a point in time or over time – Construction
- Example 18** – Measuring progress when making goods or services available – Health Clubs
- Example 19** – Uninstalled materials – Construction
- Example 53** – Non-refundable upfront fees – Services

- Example 54** – Right to use intellectual property
- Example 55** – Licence of intellectual property
- Example 57** – Franchise rights
- Example 58** – Access to intellectual property – Images
- Example 59** – Right to use intellectual property – Music
- Example 60** – Access to intellectual property – Movies

- Example 61** – Access to intellectual property – Brand
- Example 62** – Repurchase agreements
- Example 63** – Bill-and-hold arrangement

**Basis for Conclusions:**  
BC117-BC157; BC396-BC431



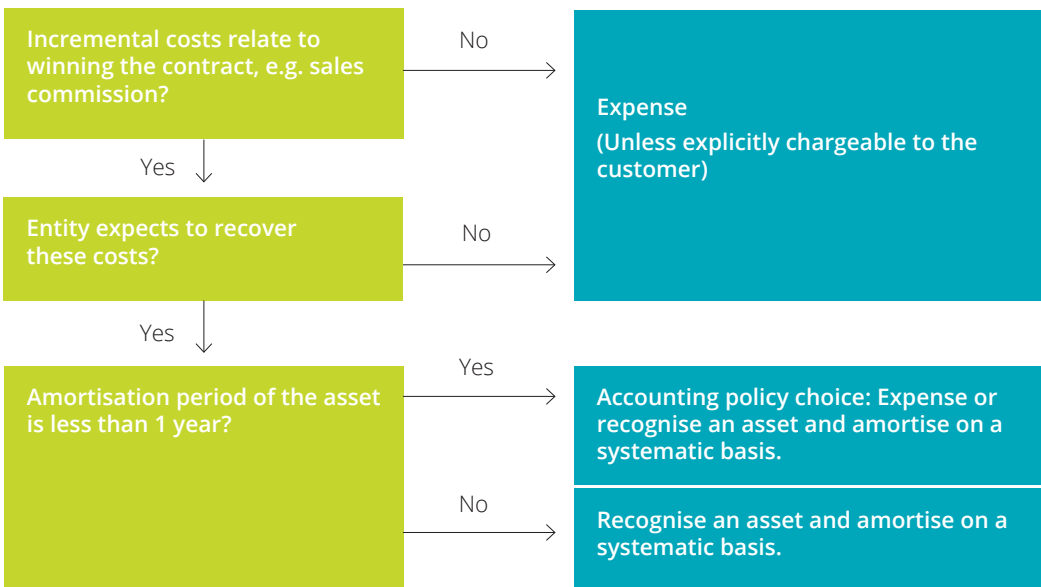
# Contract costs

The new standard introduces guidance on how to account for costs associated with a customer contract when they do not fall within the scope of another standard, e.g. AASB 102 Inventories or AASB 116 Property Plant and Equipment. The guidance addresses costs of obtaining a contract, costs of fulfilling a contract and the amortisation and impairment of contract costs capitalised.

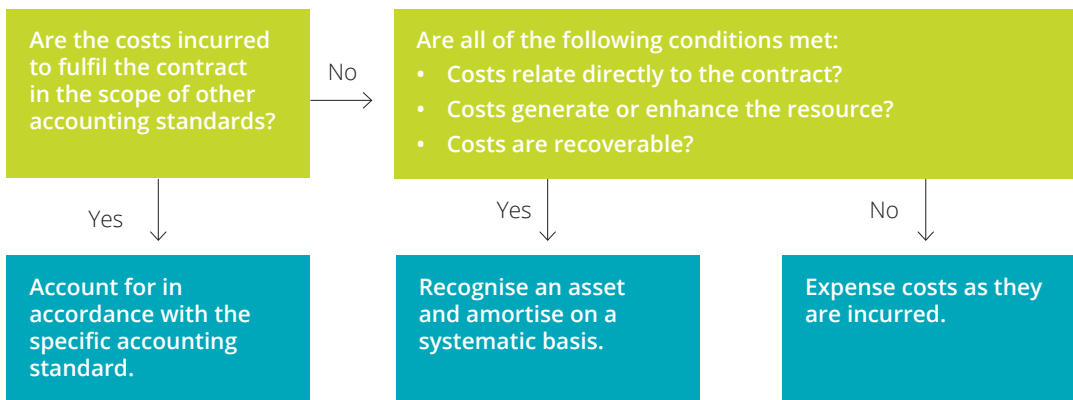
## What costs can be capitalised?

When assessing whether contract costs are eligible for capitalisation it is important to distinguish between the costs of obtaining a contract and the costs of fulfilling it. Both of these categories of cost may be eligible for capitalisation in accordance with the standard. However, the rules for each category are different and care must be taken to apply the correct guidance.

### Incremental costs of obtaining a contract [AASB 15.91-94]:



### Costs to fulfil a contract [AASB 15.95-98]:



**Costs directly attributable to a contract include [AASB 15.97]:**

- Direct labour
- Direct materials
- Allocations of costs directly related to the contract
- Costs explicitly chargeable to the customer under the contract
- Other costs directly incurred as result of entering into the contract, e.g. payments to subcontractors.

**Costs required to be expensed when incurred [AASB 15.98]:**

- General and administrative costs, unless explicitly chargeable under the contract
- Costs that relate to satisfied performance obligations
- Costs of wasted materials, labour or other contract costs.

**Amortisation of capitalised contract costs [AASB 15.99–100]:**

Costs that are recognised as assets are amortised over the period that the related goods/services are to be transferred to the customer. An entity should update the amortisation if there is a significant change in the expected timing of transfer of the remaining goods/services under the contract which will be accounted for as a change in estimate in accordance with AASB 108 Accounting Policies, Changes in Accounting Estimates and Errors.

**Contract duration [AASB 15.11–12]:**

Contract duration is an important assessment for the purpose of determining the appropriate amortisation of costs, as well as deferred revenue. Some of the factors to consider in assessing the duration of a contract are:

- Whether there are 'legally enforceable rights and obligations'
- Whether there is a reference to a fixed period in the contract
- Clauses in the contract or past practice relating to termination and auto-renewal of contracts.

**Impairment of capitalised contract costs [AASB 15.101–104]:**

Costs that are recognised as assets are periodically tested for impairment. The recoverability of capitalised contract costs should be assessed on a contract-by-contract basis by comparing the remaining consideration to the unamortised contract costs. Prior to recognising an impairment loss on the capitalised contract costs, the entity should first evaluate recovery of the carrying value of other assets related to the contract according to the guidance in other accounting standards, such as AASB 102 Inventories and AASB 136 Impairment of Assets. After recording any asset impairment from applying other standards, an entity should apply the impairment guidance in this Standard to the contract cost asset.





### To consider:

- Are the costs incurred directly attributable to the contract?
- Does the entity incur design costs prior to obtaining a contract?
- What is the duration of the contract?
- Are there options to extend the contract beyond its initial terms?
- Can the entity recover set-up or mobilisation costs incurred that are not considered separate performance obligations? Are these costs charged to the customer separately?
- How does the entity assess whether a contract is 'anticipated' for the purpose of capitalising directly attributable costs?

- The standard prohibits capitalisation of costs that are to be incurred by the entity regardless of whether a contract is won, e.g. legal, travel and other costs associated with bidding, proposal and marketing. These costs should be expensed. Costs which are incurred only due to the entity winning a contract, e.g. sales commission paid to employees, will be eligible for capitalisation if they are recoverable
- Contract costs expensed cannot be capitalised later
- For the purpose of assessing the recoverability of contract costs, an entity is required to determine the remaining consideration under the contract. In order to do so, an entity should use the transaction price determined in Step 3 without applying the constraint on variable consideration. However, an entity is required to adjust the remaining consideration for the customer's credit risk (expected provision for doubtful debts)
- The standard contemplates that an entity can capitalise costs that are directly attributable to fulfilling an 'anticipated' contract.



### AASB 15 reference:

AASB 15: 91–104

#### Illustrative Examples:

**Example 36** – Incremental costs of obtaining a contract

**Example 37** – Costs that give rise to an asset

**Basis for Conclusions:** BC297–BC311



# Disclosures

The presentation requirements of the new standard include disclosure intended to enable users to understand the amount, timing and judgements related to revenue recognition and the related cash flows. The requirements include, where applicable, qualitative and quantitative information that will extend disclosures beyond current practice.

## How will the financial statements change?

### From now until effective date of application:

Entities should consider what disclosures are required to comply with AASB 108.30–31.

For example:

- Effective date and expected date of initial application
- Expected impacts
- Nature of changes in accounting policy as a result of applying the new standard.

### Significant level of enhanced and detailed disclosure:

The new disclosure requirements encompass both quantitative and qualitative disclosures [AASB 15.110-129].

### Objective:

Enable users to understand nature, amount, timing and uncertainty of revenue and cash-flow

Contracts with customers	Assets from contract costs	Significant judgements applied
<ul style="list-style-type: none"> <li>• Disaggregation of revenue into categories that show how economic factors affect the nature, amount, timing and uncertainty of revenue and cash flows, reconciled to the Segment Note</li> <li>• Reconciliation of contract balances:               <ul style="list-style-type: none"> <li>– Opening and closing balances and revenue recognised during the period from changes in contract balances</li> <li>– Qualitative and quantitative information about the significant changes in contract balances</li> </ul> </li> <li>• Descriptive information about an entity's performance obligations</li> <li>• Information about the transaction price allocated to remaining performance obligations and when revenue will be recognised</li> <li>• Impairment losses on receivables.</li> </ul>	<ul style="list-style-type: none"> <li>• Judgements used to ascertain costs to obtain or fulfill a contract</li> <li>• Method(s) used for amortisation</li> <li>• Closing balance by main category (set-up costs, pre-contract costs, costs to obtain contracts)</li> <li>• Amount of amortisation during the period</li> <li>• Amount of impairment loss during the period.</li> </ul>	<ul style="list-style-type: none"> <li>• Judgements applied or changes in judgement regarding the:               <ul style="list-style-type: none"> <li>– Timing of satisfaction of performance obligations</li> <li>– Transaction price allocated to performance obligations</li> </ul> </li> <li>• Performance obligations satisfied over time – methods used to measure progress and the reasoning</li> <li>• Methods, inputs and assumptions for determining the transaction price; constraining variable consideration; allocation of the transaction price; obligations for refunds and returns</li> <li>• Performance obligations satisfied at a point in time – evaluation of when a customer obtains control of goods/services.</li> </ul>

## Further considerations:

### Principal vs. agent guidance impacting presentation of revenue:

An entity needs to determine whether it is the principal in the arrangement (i.e. it will provide goods/services to the customer) or it is an agent (i.e. its role is to arrange for another party to provide the goods/services). This conclusion determines whether the entity presents revenue on a 'gross' or 'net' basis. A principal recognises the 'gross' amount paid by the customer as revenue and records a corresponding expense for the commission or fee it has to pay to any agent in addition to the direct costs of satisfying the contract.

An agent records the commission or fee earned for facilitating the transfer of goods/services as revenue (i.e. the 'net' amount retained) [AASB 15.B34–36].

Indicators that an entity is acting in the capacity of an agent include the following [AASB 15.B37]:

- Another party is primarily responsible for fulfilling the contract
- The entity does not have inventory risk before or after the goods have been ordered by a customer, during shipping or on return
- The entity does not have discretion in establishing prices for the other party's goods/services and, therefore, the benefit that the entity can receive from those goods/services is limited
- The entity's consideration is in the form of a commission
- The entity is not exposed to credit risk for the amount receivable from a customer in exchange for the other party's goods/services.



### To consider:

- Does management have access to all information required to be disclosed using the entity's current systems/processes?
- What is the most efficient way to gather the required information?
- Will the information be in an auditable format?
- Is there a gap in the current systems and processes compared to what will be required?
- Based on the systems gap analysis performed, what steps will the entity undertake to change, update or implement systems and processes if required?
- Will the disclosures be sensitive and prejudicial to the business? If so, what approval procedures need to be followed?

- The Australian Securities and Investments Commission ('ASIC') has highlighted the disclosure requirements relating to 'standards issued but not yet effective' as an area of focus. Entities need to consider communication needs of various stakeholders and assess carefully the disclosures they intend to include in their financial statements for the reporting periods until the standard is effective
- Significant judgement will be required to establish what disclosures will be considered appropriate under the requirements of the new standard, including determining the level of disaggregated information
- The assessment of whether an entity acts in the capacity of a principal or agent can require application of significant judgement and may have a material impact on the amount of revenue reported
- There is no exemption in the standard to omit disclosure based on the sensitivity of information to be disclosed.



**AASB 15 reference:** AASB 15.110–129; B87–B89

**Basis for Conclusions:** BC327–BC361

# Transition

The IASB initially issued IFRS 15 with an effective date for annual reporting periods starting on or after 1 January 2017. However, due to external feedback, the IASB deferred the effective date for a year, to reporting periods starting on or after 1 January 2018. Early adoption is permitted. For Australian entities that have a 30 Jun year end, the effective date will be 1 July 2018, with the first annual reporting period ending on 30 June 2018.

## What transition approach to choose?

**AASB 15 offers three choices to transition:**

Full retrospective approach		Modified Approach Commence in year of adoption – ‘no comparatives’ but reconciliation still required [Option 3]
Retrospective approach without practical expedient [Option 1]	Retrospective approach with practical expedient [Option 2]	
<ul style="list-style-type: none"> <li>• In accordance with AASB 108 Accounting Policies, Changes in Accounting Estimates and Errors</li> <li>• Restate each prior reporting period presented before the date of initial application – 1 January 2018/1 July 2018</li> <li>• Recognise cumulative effect of initial application in equity at start of earliest comparative period presented – 1 January 2017/ 1 July 2017</li> <li>• No practical expedient</li> <li>• Disclosure for current period and each prior period presented:               <ul style="list-style-type: none"> <li>– Amount of adjustment for each line item affected</li> <li>– Updated basic and diluted earnings per share.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Restate each prior reporting period presented before date of initial application – 1 January 2018/1 July 2018</li> <li>• Recognise cumulative effect of initial application in equity at start of earliest comparative period presented – 1 January 2017/1 July 2017</li> <li>• Three optional practical expedients               <ul style="list-style-type: none"> <li>– No comparative restatement for completed contracts that begin and end within the same annual reporting period</li> <li>– Permitted use of the benefit of hindsight when assessing variable consideration for completed contracts</li> <li>– Exemption from disclosing remaining performance obligation(s) and expected timing of recognising revenue from such remaining performance obligation(s) for all comparative periods.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Recognise cumulative effect of initial application in equity at the start of the initial application period – 1 January 2018/1 July 2018</li> <li>• Comparative prior year periods are not adjusted</li> <li>• Disclose the impact of AASB 15 on each financial line item in the current period compared to what would have been recognised under the previous standards and a reason for the difference</li> <li>• Ignore contracts that were completed prior to date of initial application – 1 January 2018/ 1 July 2018.</li> </ul>

**Impacts of alternative to full retrospective approach:**

The following diagram illustrates how three different contracts would be treated using the transition methods permitted in the new standard.

For an entity with a 30 June year end:

**Contract 1:**

Begins and ends in 2017–18



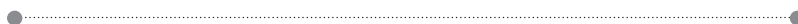
**Contract 2:**

Begins in 2015–16 and ends in 2017–18



**Contract 3:**

Begins in 2015–16 and ends in 2020–21



Date of initial application

	Retrospective approach	Modified approach
<b>Contract 1</b>	Begins and ends in same annual reporting period – practical expedient available.	Contract completed before date of initial application – do not apply AASB 15.
<b>Contract 2</b>	Adjust opening balance sheet of each affected component of equity for earliest prior period presented, 1 July 2017.	Contract completed before date of initial application – do not apply AASB 15.
<b>Contract 3</b>	Adjust opening balance sheet of each affected component of equity for earliest prior period presented, 1 July 2017.	Adjust opening balance of each affected component of equity at the date of initial application, 1 July 2018. Amounts for prior year ended 30 June 2018 are not restated. Provide explanation by each line item for the changes made.



**To consider:**

- Do the entity's current systems and processes have the capacity to generate information required under AASB 15? If not, then how quickly can the entity change its systems and processes to enable implementation of AASB 15?
- What will be the impact on five year historical earnings and revenue profile?
- Will sufficient data and accounting records be available to facilitate audit?

- An entity will need to maintain dual accounting records in order to comply with the transition disclosure requirements
  - If the modified approach is selected, then accounting records must be maintained under AASB 15 together with records under the existing accounting standards for the first year in which AASB 15 is adopted, i.e. FY 2018–19 for a June year-end entity
  - If one of the retrospective approaches are selected, then an entity must have the systems and processes in place to keep records under AASB 15 commencing from the start of the comparative period, i.e. 1 July 2017 for a June year-end entity, while continuing to maintain records under the existing accounting standards for FY 2017–18
- There are a number of factors that an entity needs to consider when choosing the appropriate transition approach, e.g. typical contract duration, system capabilities, peer group, extent of comparative information required.



**AASB 15 reference:** Appendix C

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