

Ind AS 115

Revenue from Contracts with Customers



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“The more you learn, you
learn that you still have lot
to learn”

Agenda Points

Overview and Scope

The Five Step Model

Contract Costs

Application Guidance

Presentation and Disclosures

Effective Date and Transition

Impact of Ind AS 115

Difference with Ind AS 18



Overview and Scope



Ind AS Standards – MCA notification

MCA vide notification dated 16 February 2015 has issued the Companies (Indian Accounting Standards) Rules, 2015 containing the roadmap for applicability of Ind AS for compliance by specified class of companies. The notification (to be published in the Official Gazette) has been uploaded on MCA website along with 40 Ind AS.

40 standards issued

Incorporates all relevant
IFRS, IAS, IFRIC and SIC

Has carve outs and carve ins
as compared to IFRS

Incorporates new standards
on revenues and financial
instruments

Ind AS in Phases.....

1

2

3

4

5



2016-17

Companies having Net worth above **500 cr** (excluding Banks, NBFC, Insurance Co)

2017-18

Companies having Net worth above **250 cr** and **all listed** companies (excluding Banks, NBFC, Insurance Co)

2018-19

NBFC having Net worth above **500 cr**

2019-20

All Banks, all listed NBFC companies and **NBFC** having Net worth above **250 cr**

2020-21

All Insurance Companies 2020-21

A change in mind set



Reassessment of contracts will be time consuming



Greatest impact for those that use industry based models



Transaction price allocated on a relative selling price basis



Change to model for variable consideration



Full retrospective application may require running dual systems and gathering of historic data



More extensive disclosure requirements



Potential impact on compensation arrangements

Changes to existing revenue guidance

The new revenue standard replaces all existing revenue guidance

Ind AS 115 replaces



- ☐ AS 7 Construction Contracts
- ☐ AS 9 Revenue Recognition
- ☐ ASI 14 Disclosure of Revenue from Sales Transactions
- ☐ ASI 29 Turnover in case of Contractors
- ☐ Guidance Note on Accounting for Real Estate Transactions



- ☐ Ind AS 11 Construction Contracts
- ☐ Ind AS 18 Revenue Recognition
- ☐ Appendix B (Ind AS 18) Customer Loyalty Programme
- ☐ Appendix A (Ind AS 18) Revenue- Barter Transactions involving advertising services.
- ☐ Appendix C (Ind AS 18) Transfer of Assets from Customers

Scope

Part of a Contract

Ind AS
115

Other
Ind AS



Portfolio of Contracts

Contract 1

Contract 2

Contract 3

Contract 4



De-recognition of non-
financial assets



Certain types of non-
monetary exchanges



Insurance contract



Financial instruments and
Contractual rights and
obligations in the scope of
other Ind ASs

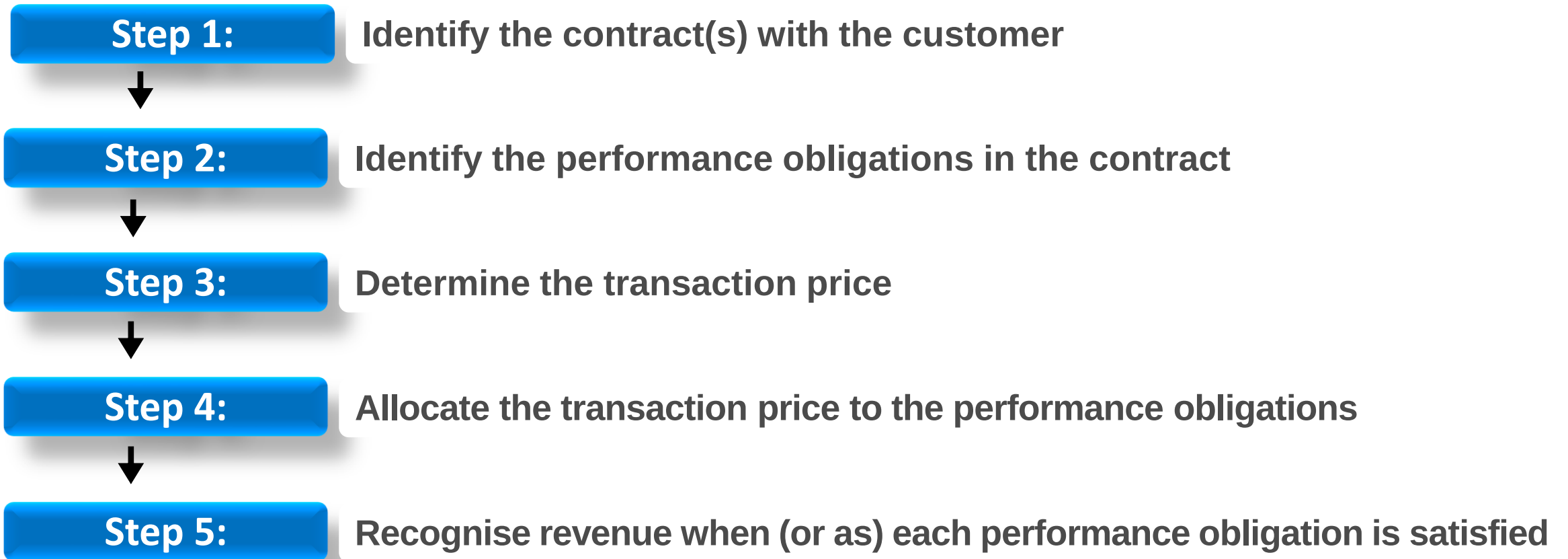


Lease contract



Summary of the model

Core principle: **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 Five Step Model

Contracts may be written, oral or implied by customary business practices, but revenue can be recognized only on those contracts that are enforceable and have commercial substance

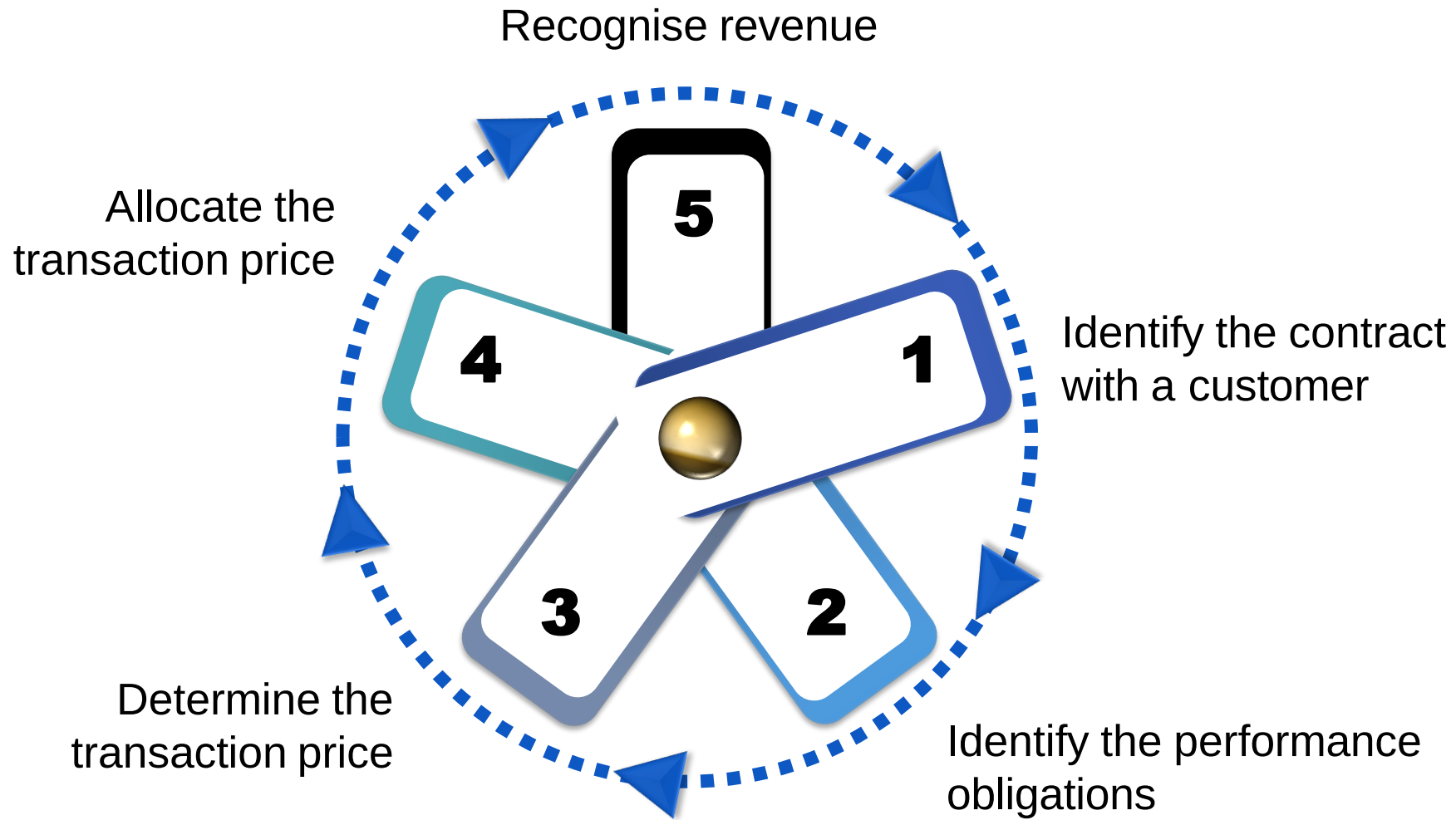
Performance obligations are explicitly or implicitly promised goods or services in a contract as well those arising from customary business practices. An entity needs to identify performance obligations which are distinct

The transaction price is the amount of consideration to which an entity expects to be entitled. It includes variable consideration, impact of significant financing components, fair value of non-cash consideration and impact of consideration payable to the customer.

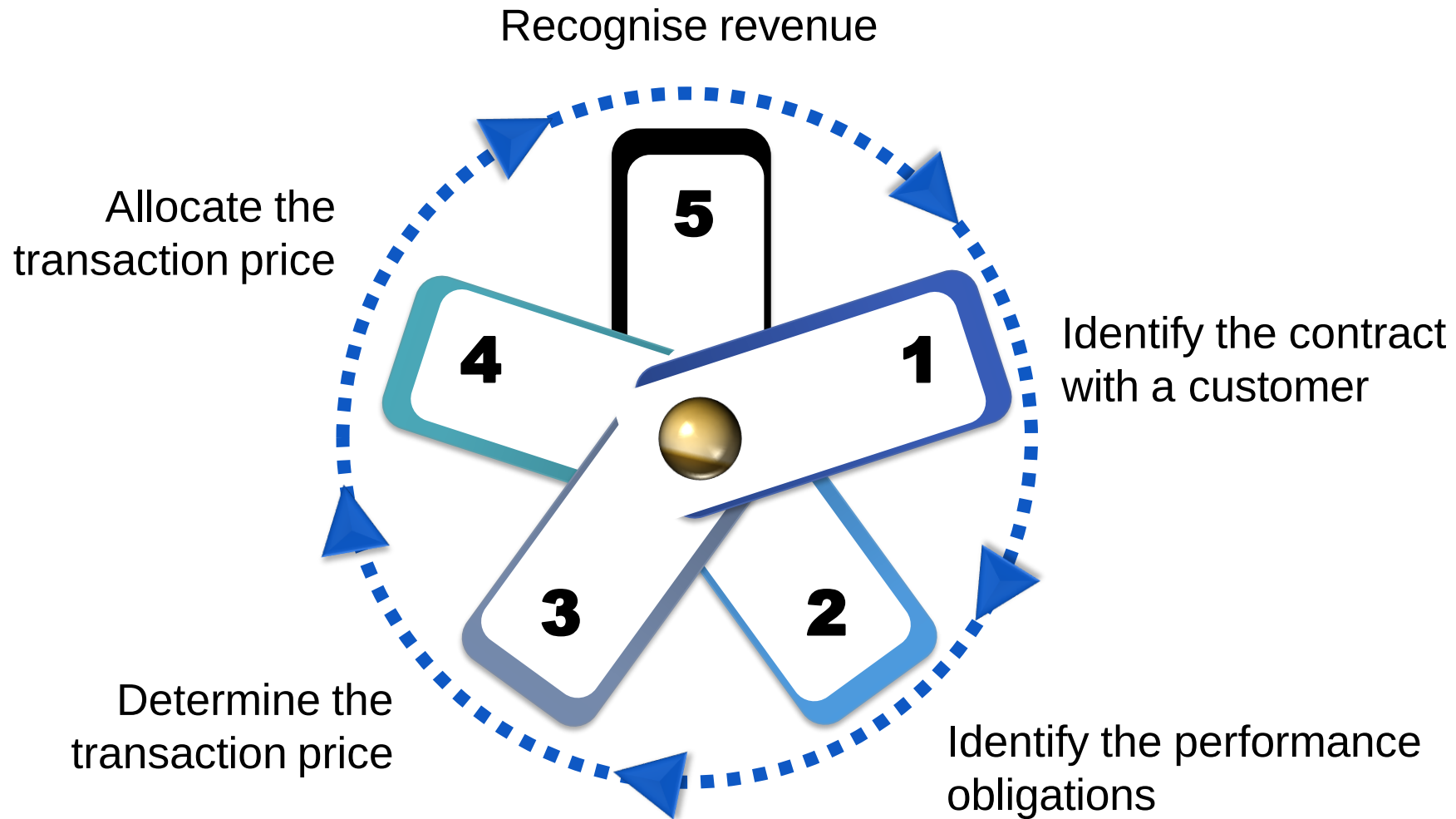
The standard requires allocation of the total contract price to the various performance obligations based on their relative stand-alone selling prices, with limited exceptions

Revenue recognition can occur either over time or at a point in time. Revenue recognition for a performance obligation occurs over time only if it meets one of the three prescribed criteria. Ind AS 115 focuses on the 'control approach' to determine revenue recognition as against the 'risk and rewards' model under Ind AS 18.

The Five Step Model Overview



The Five Step Model Overview



A contract is defined as an agreement between two or more parties that creates **enforceable rights and obligations with commercial substance**

- ☐ Can be written, oral or implied, but must meet specific criteria
- ☐ Does not exist if *both* parties can cancel without penalty



Consideration

... collection of consideration is considered probable.

Rights can be identified

... rights to goods or services and payment terms can be identified.



Commercial Sense

... it has commercial substance.

Committed to Obligation

... it is approved and the parties are committed to their obligations.



Attributes of a contract

To be within the scope of Ind AS 115, a contract with a customer should satisfy all of the following criteria:

- ☐ The parties have approved the contract and are **committed to perform their respective obligations**.
- ☐ Each party's **rights regarding the goods or services** to be transferred can be identified.
- ☐ **Payment terms** can be identified.
- ☐ The contract has **commercial substance**.
- ☐ 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.

These criteria are assessed at the inception of the arrangement



Example : Identifying a contract – free trial period

Netflix is engaged in the business of providing online movie streaming services. To encourage all potential customers to sign up for the paid subscription, it offers one month of free subscription. At the time of subscribing to the free service, the customer approves the online terms and conditions for free services. At the end of the free subscription period, a customer can either sign up for the paid services of 12 months or the free subscription will stop.

Evaluation

Revenue cannot be recognised during the trial period. A contract does not exist until the customer commits to purchase the service. The rights and obligations of the contract only include the future 12 months of paid subscription services, not the free trial period. Thus, Company A should not record revenue related to the two-month free trial period. The transaction price should be recognised as revenue on a prospective basis as the 12 months of services are transferred.

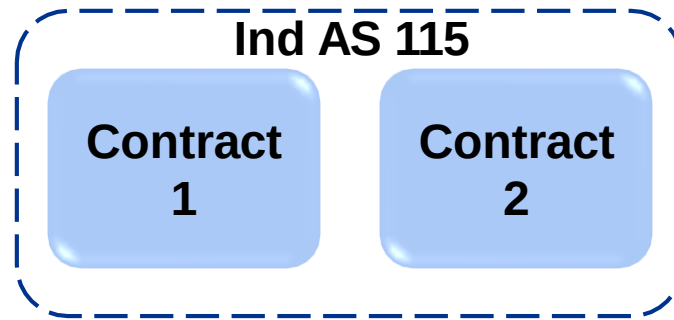
- ❑ An entity licences a patent to a customer in exchange for a usage-based royalty. At contract inception, the entity evaluates and concludes that the arrangement meets all criteria, including the collectability criterion, for identification of contract. In the first year of the contract, the customer provides quarterly reports of usage and pays within the agreed-upon period.
- ❑ During the second year of the contract, the customer continues to use the patent; however, its financial condition and credit worthiness deteriorates. The customer's current access to credit and available cash on hand are limited. The customer pays the first quarter's royalties but makes only nominal payments for the usage of the patent in quarters 2–4.
- ❑ During the third year, the customer continues to use the entity's patent. However, the customer has lost access to credit and its major customers. This results in significant deterioration of the customer's ability to pay. The entity therefore concludes that it is unlikely that the customer will be able to make any further royalty payments for ongoing usage of the patent.



Example — Collectability of the consideration - Evaluation

- ❑ **Year 1** – The entity accounts for the contract with the customer in accordance with the principles of Ind AS 115 applicable to usage-based royalty, i.e., recognise revenue when the customer's subsequent usage occurs.
- ❑ **Year 2** – Considering decline in the customer's credit worthiness, the entity reassess the arrangement and concludes that collection of the consideration is still probable. Hence, the contract continues to exist. Accordingly, the entity continues to recognise revenue when the customer usage occurs. However, it will recognise impairment of the receivables in accordance with guidance given for expected credit loss in Ind AS 109 *Financial Instruments*.
- ❑ **Year 3** – Due to significant change in facts and circumstances, the entity reassesses the contract criteria and determines that they are not met because it is no longer probable that the entity will collect the consideration. Accordingly, the entity does not recognise any further revenue. The entity also recognises any impairment of the existing receivable in accordance with Ind AS 109.

- Contracts may be combined and accounted for as a single contract.



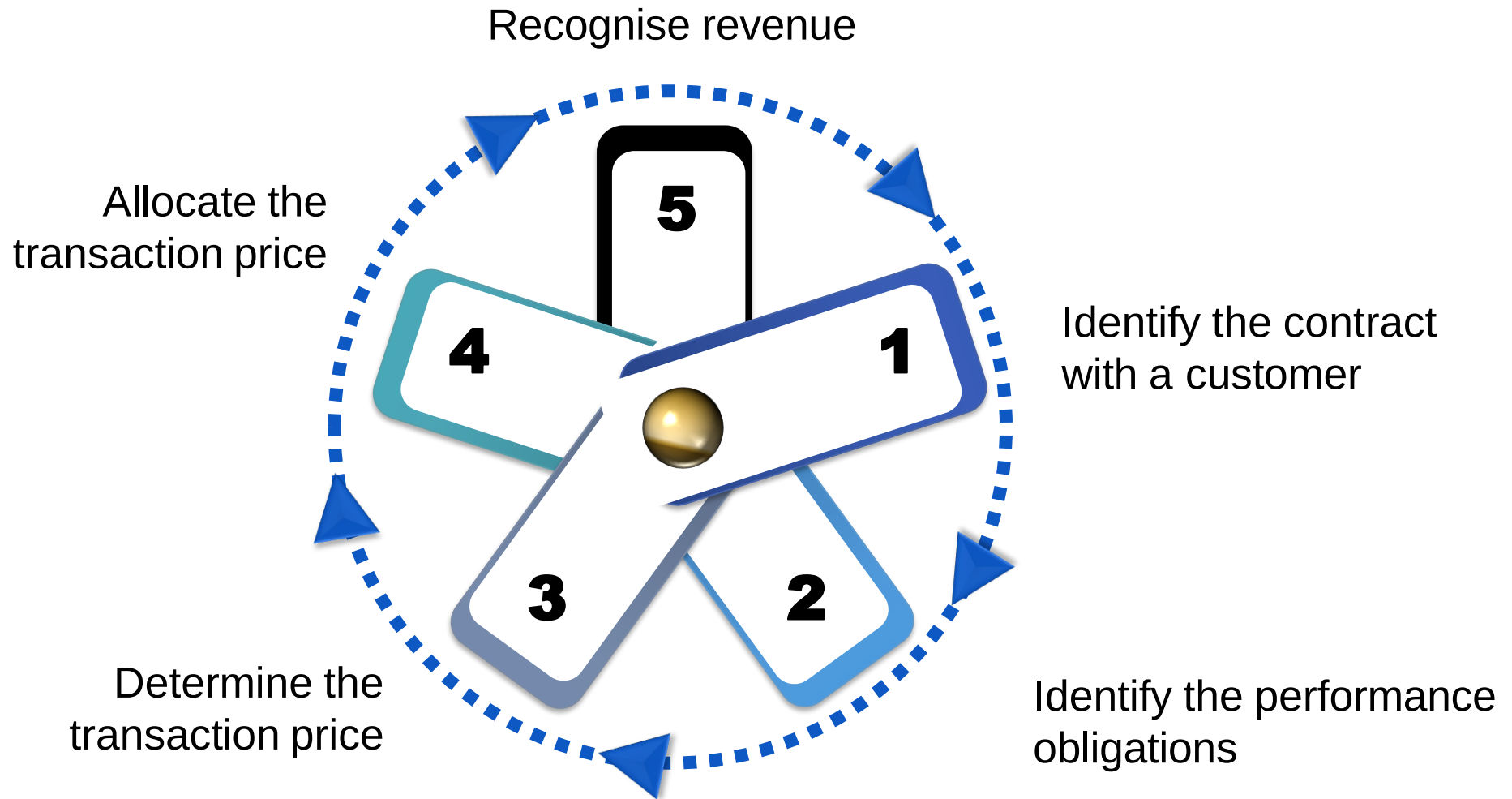
- Contracts are combined if entered into at or near the same time with the same customer and one or more of the following criteria are met.

Negotiated as package with a single commercial objective.

Consideration in one contract depends on the other contract.

Goods and services are a single performance obligation.

The Five Step Model Overview





Identifying the promised goods and services in the contract

- a) Sale of goods produced by an entity, e.g., finished goods
- b) Resale of goods purchased by an entity, e.g., traded goods
- c) Resale of rights to goods or services purchased by an entity, e.g., a ticket resale
- d) Performing a contractually agreed-upon task (or tasks) for a customer
- e) Providing a service of standing ready to provide goods or services (e.g., unspecified updates to software that are provided on a when-and-if-available basis) or of making goods or services available for a customer to use as and when the customer decides
- f) Providing a service of arranging for another party to transfer goods or services to a customer, e.g., acting as an agent of another party
- g) Constructing, manufacturing or developing an asset on behalf of a customer
- h) Granting licences
- i) Granting options to purchase additional goods or services (if option is a material right)

Identify Performance Obligations in the Contract

A performance obligation (PO) is a promise to deliver a good or service that meets **both** the following criteria

Criterion 1: Can the customer benefit from the good or service either on its own or together with other resources that are readily available to the customer?

+

Criterion 2: Is the promise to transfer the good or service separately identifiable from other promises in the contract?

Yes



Distinct performance obligation

No



Not distinct – combine with other goods and services

Exception: A series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer may be a single performance obligation.

Given below are examples of explicit/implicit promises for an entity engaged in the business of manufacturing and selling vehicles to a distributor who will then resell it to an end customer.

Explicit promise of service	In contract with the distributor, the entity promises to provide free maintenance services to the end customer purchasing a vehicle.
Implicit promise of service	The entity does not explicitly promise maintenance services in the contract. However, it has historically provided free maintenance services to end customers.
Not a promised service	The entity does not explicitly promise maintenance services in the contract. Nor has it historically provided free maintenance services. However, before sale to the end customer, it makes an offer to provide free maintenance services to the end consumer. This obligation is accounted for in accordance with Ind AS 37. In addition, for future contracts with customers, the entity should assess whether it has created a business practice resulting in an implied promise to provide maintenance services.



Single Performance Obligation?

An entity enters into a contract to build a **house** for a customer.

Potential Performance Obligations

Bricks

Windows

Fittings

Construction
service

Q: Do the goods and services individually meet the criteria?

Criterion 1 – Benefit on its own



Each material could be used
with another readily available
item.

**Criterion 2 – Good or service
separately identifiable**



Entity is providing a significant
integration service.



Example: Distinct goods or services - customer benefits from the good or service

A manufacturer enters into a contract with a customer to sell a custom tool and replacement parts manufactured for the custom tool. The manufacturer only sells custom tools and replacement parts together, and no other entity sells either product. The customer can use the tool without the replacement parts, but the replacement parts have no use without the custom tool.

Evaluation

There are two performance obligations if the manufacturer transfers the custom tool first because the customer can benefit from the custom tool on its own and the customer can benefit from the replacement parts using the custom tool previously transferred to it. However, there is only one performance obligation if the manufacturer transfers the replacement parts first, because the customer cannot benefit from those parts without the custom tool.

- Customer contract for a sale of a machine and **standard installation**.
- Installation services are also offered by third party providers.

Potential Performance Obligations

Machine

Installation

Q: Does the machine meet the performance obligation criteria?

Criterion 1 – Benefit on its own



Machine can be used with other available inputs.

I.e. third party installation.

Criterion 2 – Good or service separately identifiable



No significant integration service, because installation is a standard service.



Multiple Performance Obligations?

Example

- ☐ Daikin enters into a contract to manufacture and install customised equipment and provide maintenance services for a five-year period
- ☐ Installation services include the integration of multiple pieces of equipment at the customer's facility in order for the equipment to operate as a single unit
- ☐ Equipment cannot operate without installation
- ☐ Entity sells equipment and installation services together; does not sell installation separately
- ☐ Other vendors can provide the installation services
- ☐ The maintenance services are sold separately

Multiple Performance Obligations?

	Step 1 – Capable of being distinct	Step 2 – Distinct in the context of the contract
Equipment	Good cannot be used without installation, but customer can obtain installation from another source. Good is distinct. Move to Step 2.	Equipment and installation are highly interrelated. Significant customisation is required during installation. Good isn't distinct on its own because it must be combined with installation.
Installation	Installation can be provided by multiple vendors, so service is distinct. Move to Step 2.	See discussion above. Equipment and installation are not distinct from one another.
Maintenance	Services have a distinct function because they are sold separately. Move to Step 2.	Services are not highly interrelated. No integration, modification or customisation required. Services are individually distinct.

In this example, there are two performance obligations: (1) the equipment and the installation because they are distinct within the context of the contract; (2) maintenance services because they are distinct services.

Example

- ❑ Microsoft enters into a contract with a customer to provide a perpetual Windows software license, installation services, and three years of post contract customer support (unspecified future upgrades and telephone support).
- ❑ The installation services require the entity to configure certain aspects of the software, but do not significantly modify the software.
- ❑ These services do not require specialized knowledge; and other sophisticated software technicians could perform similar services.
- ❑ The software does not require the upgrades and telephone support in order for it to remain functional.

How many performance obligations are there in the contract?

Solution

- ❑ Performance obligations are- Windows software license, installation services, unspecified future upgrades and telephone support.
- ❑ The customer can benefit from the Windows software (delivered first) because it is functional without the installation services, unspecified future upgrades/ telephone support.
- ❑ The customer can benefit from the subsequent installation services, unspecified future upgrades and telephone support together with the software, which it has already obtained.
- ❑ Microsoft concludes that each good and service is separately identifiable because the installation services, unspecified future upgrades, and telephone support do not significantly modify or customize the software. Additionally the software and services are not being integrated into the output that the customer has contracted to receive.



Customer options to acquire additional goods and services

Does the contract grant the customer the option to acquire additional goods or services?

Does the option provide a material right to the customers that it would not receive without entering into the contract ?

NO

YES

Option is not a separate performance obligation

Option is a separate performance obligation

- ❑ Revenue is recognised when future goods and services are transferred or when the option expires
- ❑ The transaction price is allocated to performance obligations (including the option) based on relative stand-alone selling prices
- ❑ Estimate of stand-alone selling price of option reflects:
 - The discount a customer receives when exercising the option, adjusted for the discount a customer receives without exercising the option and the likelihood the option will be exercised
- ❑ As an alternative to estimating the stand-alone selling price of the option, an entity could evaluate the transaction assuming the option will be exercised
 - Transaction price will be determined by including any consideration estimated to be received from the optional goods and services (variable consideration)
 - Transaction price would be allocated to all goods and services (including those under option)
 - Typically applied when original and additional goods are similar

Example

- ❑ An entity enters into a contract with a customer A to sell garden supplies, and the arrangement includes a 40% discount voucher on future purchases
- ❑ Simultaneous seasonal promotion gives all customers a 10% discount, therefore, customer A receives an incremental discount of 30% (40% discount in the contract less the 10% discount available to all customers)
- ❑ Entity determines there is an 80% likelihood of redemption and estimates that customers will purchase (on average) INR 50 of additional goods

Solution

Entity estimates the stand-alone selling price of voucher as:

- ❑ Average purchases x incremental discount x likelihood
- ❑ $\text{INR } 50 \times (40\% - 10\%) \times 80\% = \text{INR } 12$



Customer options to acquire additional goods and services

Example

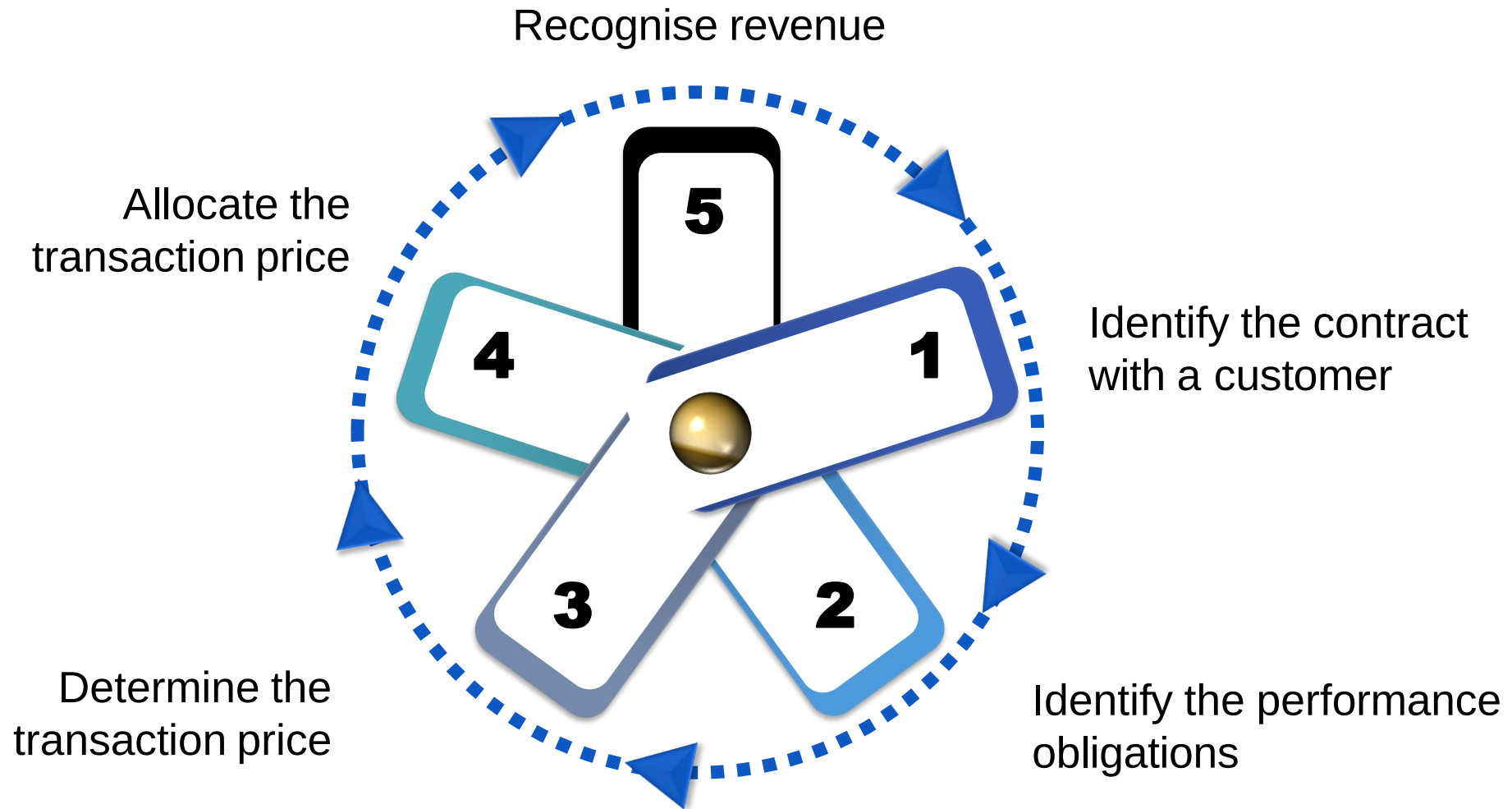
- ❑ Gold Gym sells gym memberships for INR 25000 per year, with an option to renew at a discount in years two and three at INR 20000 per year
- ❑ Entity obtains 100 new customers under the promotion
- ❑ Entity estimates an annual attrition rate of 50%

Solution

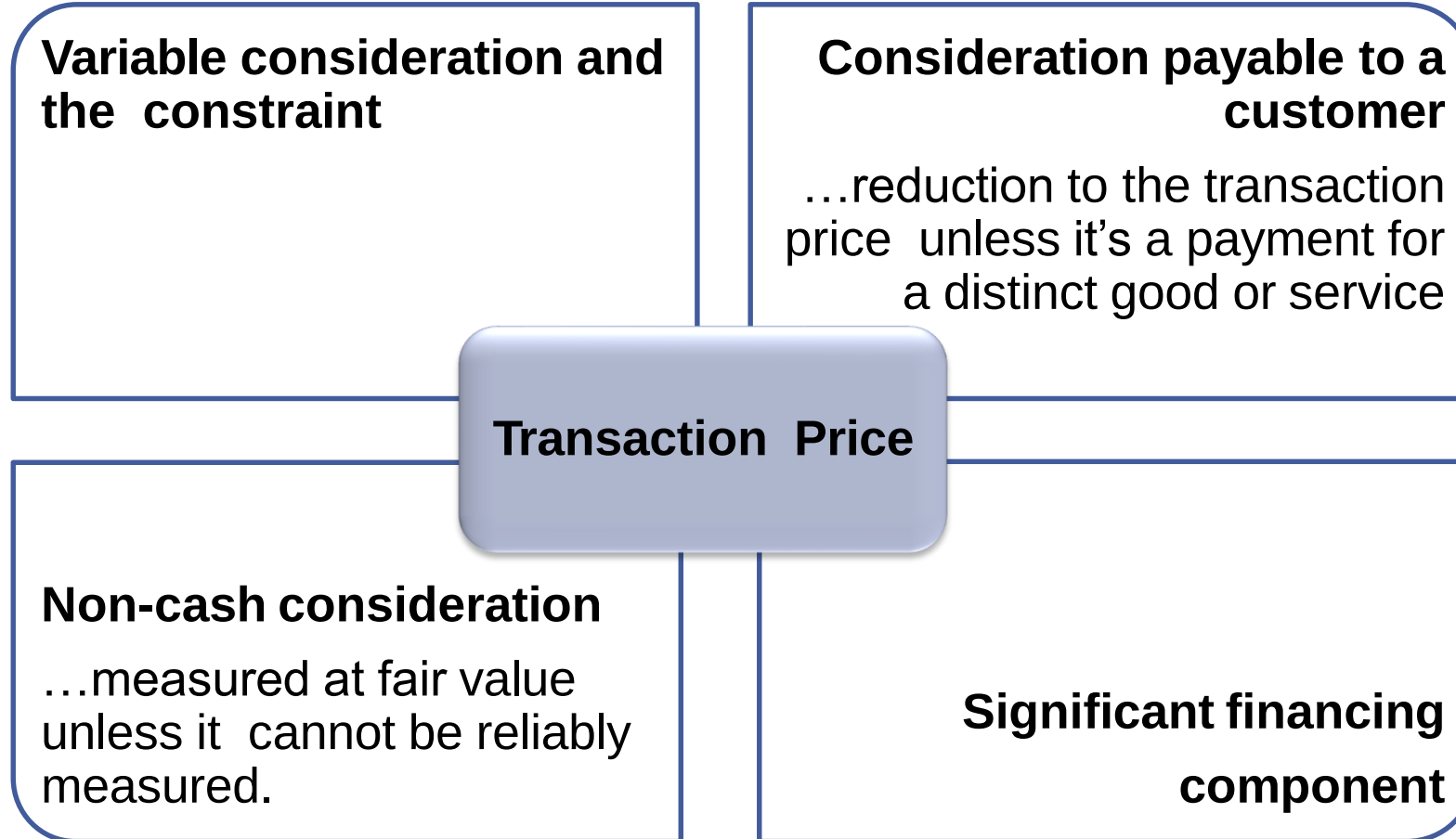
Allocated price per unit (year) is calculated as follows:

- ❑ Total estimated consideration / total estimated memberships sold
- ❑ Total estimated memberships is 175 members
 - (Year 1 = 100; Year 2 = 50; Year 3 = 25) = 175
- ❑ Total consideration is INR 40,00,000
 - $(100 \times \text{INR } 25000) + (50 \times \text{INR } 20000) + (25 \times \text{INR } 20000) = \text{INR } 40,00,000$
- ❑ Allocated price per membership is INR 22,857 ($\text{INR } 40,00,000 / 175$)

The Five Step Model Overview



Determine the Transaction Price



Exception: Variable consideration is not estimated for sales – or usage- based royalties on licenses of intellectual property.

Ind AS 115 includes a general principle that an entity will determine the transaction price exclusive of amounts collected on behalf of third parties. In India, an entity collects GST on behalf of the Government and not on its own account. Hence, GST is excluded from the transaction price. However, similar clarity may not exist for excise duty and production taxes collected in various jurisdictions.



Variable consideration can be

Discounts

Credits

Incentives

Performance
bonuses

Many more...

Variable consideration is estimated using most appropriate method of either:

Expected Value

Most Likely Amount

- ❑ **Right to return:** Variable consideration includes variability resulting from refunds or returns. A contract to provide a customer with 100 widgets at a fixed price per widget contains a variable component if the customer has a right to return the widgets.
- ❑ **Volume discount:** An entity sells Product A at INR 100 per unit. If the customer purchases more than 1,000 units in a financial year, the price per unit is retrospectively reduced to INR90 per unit.
- ❑ **Implicit price concession:** An entity sells 1,00,000 units of a prescription drug to a customer for promised consideration of INR 100 million. This is the entity's first sale to a customer in a new region, which is experiencing economic difficulties. The entity expects that the region's economy will recover and determines that a relationship with this customer can help it to forge relationships with other potential customers in the region. The entity expects that it may provide a price concession. The contract contains an implied price concession and consideration is variable.

- ❑ **Penalty:** Where a penalty is inherent in determination of the transaction price, it forms part of variable consideration. An entity agrees to transfer control of a good or service in a contract with customer at the end of 30 days for INR 100,000. However, if the period exceeds 30 days, the entity will be entitled to receive only INR 95,000. In this case, the reduction of INR5,000 will be regarded as variable consideration. In other penalty cases, the transaction price may be considered as fixed

Common types and events that cause consideration to be variable

Performance, Bonuses, Incentive payments, Penalties, Refunds, Market-based fees, Discounts, Returns, Money-back guarantees, Price concessions, Volume rebates, Service level agreements, Liquidating damages, Change orders, Claims, Success fees

Contract to build a jet for a customer. The transaction price includes:

- Fixed amount: INR 100 lacs
- Completion bonus: INR 100 lacs if completed two months prior to a specified date.
- Performance bonus: INR 0 – INR 100 lacs depending on the number of flights in its first 12 months of service.

Q: How would the entity estimate variable consideration?

Fixed Amount

Not Variable

Completion Bonus

Most likely
amount

Performance Bonus

Expected value

Application

Transaction price – include the amount that is ‘highly probable’ will not result in significant revenue reversal.

Qualitative Assessment

- ☐ The risk of a reversal arising from an uncertain future event.
- ☐ The magnitude of the reversal if the uncertain event occurs.



Determine the transaction price - Variable consideration

Examples

- ❑ Entity enters into a contract and will receive a INR 100,000 performance bonus if specified performance targets are met
- ❑ Entity estimates 80% likelihood it will receive entire performance bonus and 20% likelihood it will receive none of the bonus

Solution

The new revenue recognition standard

- ❑ Due to the binary nature of the outcome, Entity determines that the best predictor of the ultimate consideration it will receive is the 'most likely amount' approach
- ❑ Therefore, INR 100,000 is included in the transaction price
- ❑ Constraint likely has no effect because Entity concludes it is probable that the bonus will be received

Examples

Entity enters into a contract and will receive a performance bonus **up to** INR 100,000 if it meets specified performance targets. It estimates the likelihood of achieving the targets as:

Possible outcomes	Probability	Calculated amount
INR 100,000	10%	INR 10,000
INR 80,000	30%	INR 24,000
INR 60,000	35%	INR 21,000
INR 40,000	10%	INR 4,000
-	15%	-
		INR 59,000

Solution

- ☐ 'Expected value' approach is determined to be the best method, Entity calculates INR 59,000 using this method
- ☐ However, Entity must consider whether any of the INR 59,000 needs to be constrained

Examples

Entity enters into a contract and will receive a performance bonus **based on five potential amounts** if specified targets are met. It estimates the likelihood of achieving the targets, as follows:

Possible outcomes	Probability	Calculated amount
INR 100,000	15%	INR 15,000
INR 80,000	30%	INR 24,000
INR 60,000	30%	INR 18,000
INR 40,000	10%	INR 4,000
-	15%	-
		INR 61,000

Solution

- ☐ 'Expected value' approach is determined to be the best method, Entity calculates INR 61,000 using this method
- ☐ Constraint limits bonus to INR 60,000 until it is probable that the next bonus level will be achieved



Determine the transaction price - Variable consideration

Example

Company A supplies components to industrial customers. The contract stipulates that the price per component will decrease per unit as sales volume increases within the stipulated period of time as follows:

Price per unit	Sales volume
Rs.100	0 -1,000,000 units
Rs.90	1,000,000 - 3,000,000 units
Rs.85	3,000,001 units and above

How is revenue estimated under Ind AS 115?



Determine the transaction price - Variable consideration - Expected value method

Solution

- ❑ A estimates probability-weighted variable consideration based on the range of possible outcomes and probabilities of each outcome.
- ❑ All possible outcomes are required to be assessed and quantified

Probability	Sales volume (units)	Price/ unit (Rs.)	Probability weighted Sales value (Rs.)	Probability weighted Sales volume (units)
10%	8,00,000 units	100	80,00,000	80,000
70%	25,00,000 units	90	157,500,000	17,50,000
20%	35,00,000 units	85	59,500,000	7,00,000
			A= 225,000,000	B= 2,530,000

- ❑ Avg unit price = Rs.88.93 (A/B). Revenue is recognised at Rs.88.93 for each unit sold. For the first 1,000,000 units sold, liability is accrued at Rs.11.07 (100-88.93) per unit, reversed upon subsequent sales.



Determine the transaction price - Variable consideration - Most likely method

Example

- ❑ Consider the following change in fact pattern:

A believes that the total sales volume for the year will be 2.5 million based on past experience and forecasted sales.

- ❑ Based on the most likely method, the transaction price is calculated as follows:

Rs.90 per unit X 2,500,000 units	Rs. 225,000,000
----------------------------------	-----------------

- ❑ Average unit price = Rs.90
- ❑ Revenue is recognised at 90 per unit for each unit sold.
- ❑ For the first 1,000,000 units sold, liability is accrued at Rs.10(100-90) per unit.



Significant Financing Component

Significant financing component

- Transaction price compared to cash selling price.
- Period between payment and delivery.
- Other reasons for payment terms.

Discount rate

- Rate that would be used in separate financing transaction between the entity and customer.

Practical Expedient

- No adjustment required if the period between performance and payment is 12 months or less.



Determine the transaction price - Significant financing component

- ☐ Reflected as an adjustment to the transaction price when significant and the primary purpose of the payment terms is to provide financing to one party in the contract
- ☐ Evaluation is not required if customer is expected to pay within one year of when control of the good or service is transferred
- ☐ If the financing component is not significant to the individual contract, entity is not required to adjust the transaction price
- ☐ Entity would use a financing rate that reflects the borrower's credit risk and expected term of the financing set at inception
- ☐ Effect of financing to be reflected separately from revenue



Determine the transaction price - Advance payment

Example

- ☐ An entity enters into a contract with a customer to sell an asset.
- ☐ Control of the asset will transfer to the customer in 2 years (ie the performance obligation will be satisfied at a point in time).
- ☐ The contract includes two alternative payment options:
 - ☐ Payment of Rs.5,000 at the end of 2nd year when the customer obtains control of the asset; or
 - ☐ Payment of Rs.4,000 when the contract is signed.
- ☐ The entity's incremental borrowing rate is 6%

How should the financing component of the arrangement be accounted for under Ind AS 115?



Determine the transaction price - Advance payment

Solution

- ❑ In case the customers opt to pay advance payment upon signing, it seems that the contract contains a significant financing component because:
 - ❑ The difference between the amount of consideration under the two options is significant (5,000 minus 4,000 ie 1,000)
 - ❑ The expected length of time between payment of advance and transfer of goods is significant (2 years)
 - ❑ The interest rate implicit in the payment options (11.8%) is significantly higher than the entity's incremental borrowing rate (6%)



Determine the transaction price - Advance payment

The following journal entries illustrate the accounting under Ind AS 115

Entry	Dr(Rs.)	Cr(Rs.)
Upon receipt of the advance on signing of the agreement:		
Cash	4,000	
Contract liability		4,000
Over the 2 year period until the asset is sold:		
Interest expense (4,000@ 6% for 2 years)	494	
Contract liability		494
Recognize revenue for transfer of assets:		
Contract liability	4,494	
Revenue		4,494



Determine the transaction price - Non-cash consideration

- ☐ When an entity expects to receive non-cash consideration, such consideration is measured at the fair value of the amounts received or promised and is included in the transaction price
- ☐ If the fair value cannot be reliably estimated, non-cash consideration is to be measured indirectly by reference to the selling price of the goods or services transferred to the customer
- ☐ If the non-cash consideration promised is variable for reasons other than just the form of non-cash consideration, the constraint on variable consideration should be applied
- ☐ For example, the constraint would not be applied to consider changes in the fair value of inventory to be received as non-cash consideration



Determine the transaction price - Consideration payable to a customer

Example

- ☐ Entity enters into a contract with a customer for the exclusive supply of paint for a three-year period
- ☐ Entity makes a INR 50,000 upfront payment, which the customer will use to customise its paint sprayers for the entity's product
- ☐ Entity determines the upfront payment is not in respect of or for a distinct good or service
- ☐ INR 50,000 is accounted for as a reduction of the transaction price
- ☐ Entity estimates INR 1,000,000 in sales with the customer over the three-year period
- ☐ The upfront payment is deferred and recognised as a reduction of revenue (in proportion to estimated sales) over the contract term



Determine the transaction price - Consideration payable to a customer

Entity determines whether amounts paid or payable to the customer (e.g., cash, credit) are:

- ☐ A reduction of the transaction price and revenue
- ☐ A payment for distinct goods and services
- ☐ A combination of the two
- ☐ For an entity to treat the consideration payable to a customer as something other than a reduction of revenue, the goods and services from the customer must be 'distinct'
- ☐ Reductions to the transaction price occur at the later of when:
 - ☐ The entity recognises revenue for the transfer of control of the goods or services to the customer
 - ☐ The entity pays or promises to pay the consideration

For the first quarter

- ❑ Q1 sales = INR 100,000
- ❑ Entity continues to estimate INR 1M in sales
- ❑ $\text{INR } 100,000 / \text{INR } 1.0\text{M} = 10\%$ of estimated sales
- ❑ $10\% \times \text{INR } 50,000 \text{ upfront payment} = \text{INR } 5,000$ to be recognised in Q1
- ❑ Entity recognises revenue of INR 95,000
(INR 100,000 actual sales - INR 5,000 consideration paid to the customer)

For the second quarter

- ❑ Q2 sales = INR 125,000
- ❑ Entity updates its estimates of total sales over the contract to INR 1.5M
- ❑ $\text{INR } 225,000 \text{ total sales to date} / \text{INR } 1.5\text{M estimated total sales} = 15\%$
- ❑ $15\% \times \text{INR } 50,000 \text{ upfront payment} = \text{INR } 7,500 - \text{INR } 5,000 \text{ recognised in Q1} = \text{INR } 2,500$ to be recognised in Q2
- ❑ Entity recognises revenue of INR 122,500 for Q2
(INR 125,000 actual sales - INR 2,500 consideration paid to the customer)



Determine the transaction price - Consideration payable to a customer

Example

- ❑ Producer sells energy drinks to Retailer, a convenience store. Producer also pays Retailer a fee to ensure that its products receive prominent placement on store shelves.
- ❑ The fee is negotiated as part of the contract for sale of the energy drinks.

How should Producer account for the slotting fees paid to Retailer?

Solution

- ❑ Producer should reduce the transaction price for the sale of the energy drinks by the amount of slotting fees paid to Retailer.
- ❑ Producer does not receive a good or service that is distinct in exchange for the payment to Retailer.



Determine the transaction price - Consideration payable to a customer

Example

- ❑ Samsung India sells 1,000 phones to Retailer for Rs.10,00,000. The contract includes an advertising arrangement that requires Samsung to pay Rs.100,000 toward a specific advertising promotion that Retailer will provide.
- ❑ Retailer will provide the advertising on strategically located billboards and in local advertisements.
- ❑ Samsung could have elected to engage a third party to provide similar advertising services at a cost of Rs.100,000.

How should Samsung account for the payment to Retailer for advertising?



Determine the transaction price - Consideration payable to a customer

Solution

- ☐ Samsung should account for the payment to Retailer consistent with other purchases of advertising services.
- ☐ The payment from Samsung to Retailer is consideration for a distinct service provided by Retailer and reflects fair value.
- ☐ The advertising is distinct because Samsung could have engaged a third party who is not its customer to perform similar services.
- ☐ The transaction price for the sale of the phones is Rs.10,00,000 and is not affected by the payment made by Retailer.



Determine the transaction price - Non-refundable upfront fees

- ☐ Entities may receive payments from customers before goods or services are provided
- ☐ In many cases, upfront payments are non-refundable
- ☐ Entities must evaluate whether non-refundable upfront fees relate to the transfer of a (future) good or service
- ☐ Fees charged for set-up activities – do not depict the transfer of services to a customer and should be ignored when measuring progress of an entity's performance
- ☐ The existence of a non-refundable upfront fee may indicate the arrangement includes an option for additional goods or services (e.g., renewal option for future goods or services at a reduced price)



Determine the transaction price - Non-refundable upfront fees

Example

- ❑ Fit-Co operates health clubs. Fit-Co enters into contracts with customers for 1 year access to any of its health clubs. The entity charges an annual membership fee of Rs.6,000 as well as a Rs.1,500 non-refundable joining fee.
- ❑ The joining fee is to compensate, in part, for the initial activities of registering the customer.
- ❑ Customers can renew the contract each year and are charged the annual membership fee of Rs.6,000 without paying the joining fee again.
- ❑ If customers allow their membership to lapse, they are required to pay a new joining fee.

How should Fit-Co account for the non-refundable joining fees?

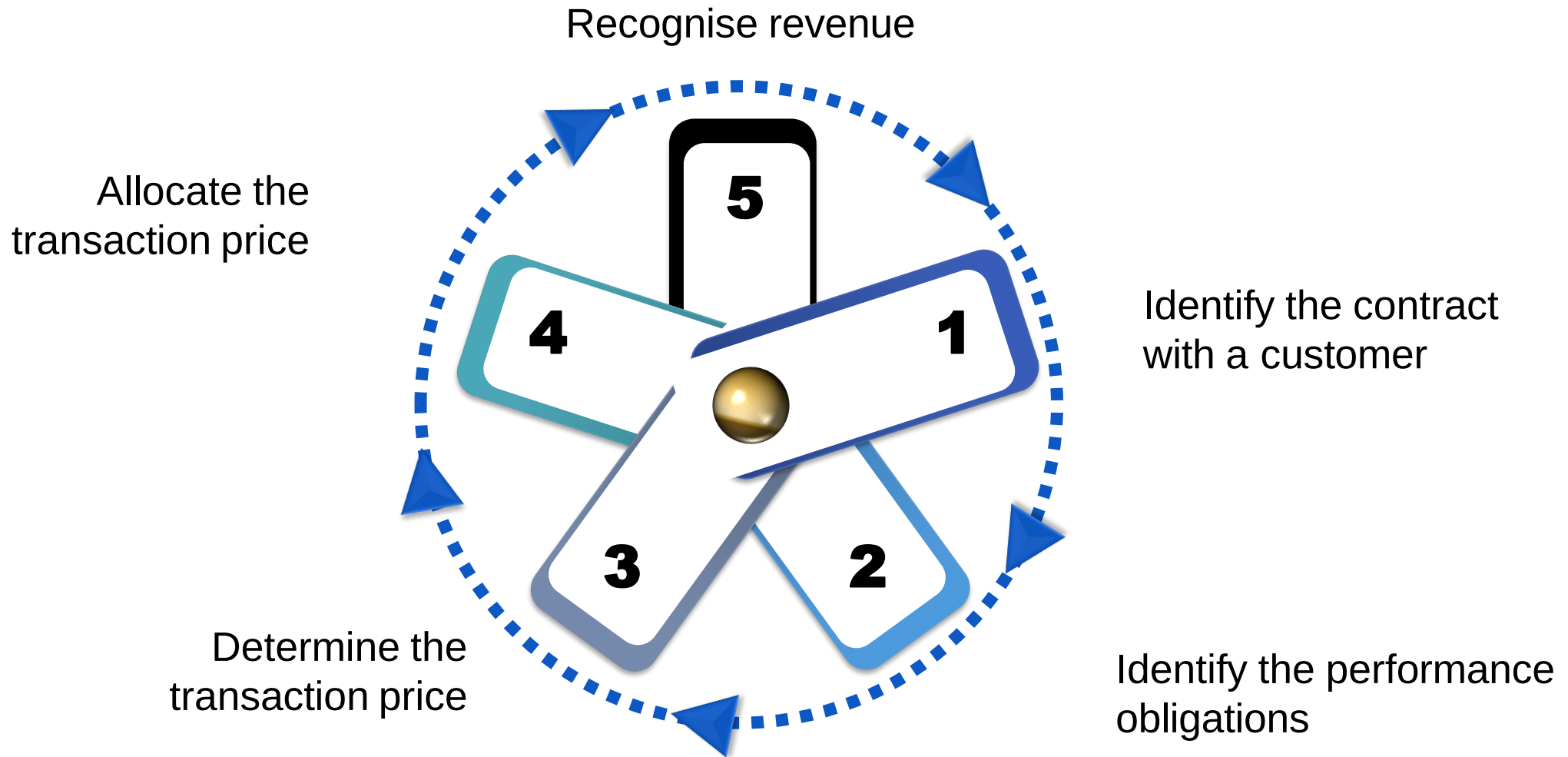


Determine the transaction price - Non-refundable upfront fees

Solution

- ❑ The customer does not have to pay the joining fee if the contract is renewed and has therefore received a material right. That right is the ability to renew the annual membership at lower price than the range of prices typically charged to new customers.
- ❑ The joining fee is included in the transaction price and allocated to the separate performance obligations, i.e. providing access to health clubs and the option to renew the contract, based on their standalone selling prices.
- ❑ Fit-Co's activity of registering the customer is not a service to the customer and therefore does not represent satisfaction of a performance obligation.
- ❑ The amount allocated to the right to access the health club is recognized over the first year, and the amount allocated to the renewal right is recognized when that right is exercised or expires.
- ❑ Fit-Co may allocate the transaction price to the renewal right by reference to the future services expected to be provided and the corresponding expected consideration.
- ❑ For e.g., if Fit-Co determines that a customer is expected to renew for an additional 2 years, then the total consideration would be Rs.19,500 (1,500 joining fee and 18,000 annual membership fees). Fit-Co would recognize this amount as revenue rateably as services are provided over the 3 years.

The Five Step Model Overview



Allocate the Transaction Price to Performance Obligations

Allocate based on relative stand-alone selling prices

Performance obligation 1

Performance obligation 2

Performance obligation 3

Determine stand-alone selling prices

Best evidence

Observable price

If not available

Estimate price

Adjusted market
assessment
approach

Expected cost plus
a margin approach

Residual approach only if selling price is
highly variable or uncertain

Contractual price or Fair value
measurement **X**



Allocate the transaction price to performance obligations

- ☐ Stand-alone selling price – price at which an entity would sell a good or service separately to a customer
- ☐ Best evidence is stand-alone sales of a good or service
- ☐ When an entity doesn't sell the good or service separately, it is required to estimate the stand-alone selling price
- ☐ Maximise the use of observable inputs
- ☐ Apply estimation methods consistently for goods/services and customers with similar characteristics
- ☐ Standard describes three estimation methods but others are permitted (and a combination of estimation methods is allowed)
- ☐ Stand-alone selling prices used to perform the initial allocation are not updated after contract inception

A two year mobile phone contract where two performance obligations are identified; 1) phone and 2) data, calls and texts.

- Total transaction price = INR 6500.
- Price of the phone on the maker's website = INR 3500.
- The entity sells a twelve month plan without a phone that includes the same level of data, calls and texts for INR 150 per month = INR 3600 (24 x INR 150).

Q: What methods could the entity use to allocate the transaction price?

Observable
price



Adjusted
market



Cost plus



Residual



Phone allocation – $\text{INR } 6500 \times (\text{INR } 3500 / \text{INR } 7100) = \text{INR } 3200$
Data, calls and texts – $\text{INR } 6500 \times (\text{INR } 3600 / \text{INR } 7100) = \text{INR } 3300$

- ❑ Entity enters into an agreement to sell hardware, professional services and maintenance services for INR 200,000
- ❑ Entity determines that each of the promised goods or services represents a separate performance obligation
- ❑ Because the entity frequently sells professional services and maintenance on a stand-alone basis, it uses those transactions to determine stand-alone selling prices of INR 25,000 and INR 15,000, respectively
- ❑ The entity rarely sells the hardware on a stand-alone basis, so it estimates the stand-alone selling price at INR 185,000 based on the hardware's underlying cost, the entity's targeted cost and the amount of margin the entity believes the market will bear (i.e., the expected cost plus a margin approach)



Allocate the transaction price to performance obligations

Performance obligation	Estimated stand-alone selling price (INR)	% of relative selling price	Allocated discount (INR)	Allocation of transaction price (INR)
Hardware	1,85,000	82.2	(20,600)	1,64,400
Professional services	25,000	11.1	(2,800)	22,200
Maintenance services	15,000	6.7	(1,600)	13,400
Total	225,000	100.0	(25,000)	200,000

Example

- ☐ Assume the same facts as Example 1, except the arrangement also includes software for a total fee of INR 250,000
- ☐ The entity determines the software deliverable is also a separate performance obligation
- ☐ The entity never sells the software on a stand-alone basis
- ☐ The entity has bundled the software into a number of different arrangements, with the pricing for that element ranging from INR 15,000 to INR 125,000



Allocate the transaction price to performance obligations

Calculation of the stand-alone selling price of the software using the residual approach

Total arrangement consideration	INR 250,000
Less estimated stand-alone selling prices:	
Hardware	(185,000)
Professional services	(25,000)
Maintenance services	<u>(15,000)</u>
Stand-alone selling price of software	<u>25,000</u>



Allocate the transaction price - Exceptions for variable consideration

- ☐ Variable consideration is required to be allocated to one or more (but not all) performance obligations, if both of the following criteria are met:
- ☐ The contingent payment relates specifically to the entity's efforts to satisfy that performance obligation
- ☐ The amount allocated entirely to that performance obligation is consistent with the overall principle for allocating consideration
- ☐ This exception can be applied to a single performance obligation or a combination of performance obligations
- ☐ Subsequent changes in variable consideration should be allocated in a consistent manner



Allocate the transaction price - Exceptions for variable consideration

Example

- ☐ Assume the same facts as in Example earlier, except that the contract price will include a INR 10,000 premium if professional services are provided within seven days of the delivery date of the hardware and software
- ☐ The customer's business is highly seasonal, and this arrangement coincides with its busiest time of year
- ☐ The professional services are more valuable to the customer if they are rendered as soon as possible
- ☐ The variable consideration relates specifically to the entity's efforts to satisfy the professional services performance obligation
- ☐ The amount of the premium allocated to professional services is consistent with the overall principle for allocating consideration

Performance Obligation	Allocated Fixed Transaction Price (INR)	Variable revenue	Total transaction price
Hardware	185,000		185,000
Software	25,000		25,000
Professional services	25,000	10000	35,000
Maintenance services	15,000		15,000
	250,000		260,000

Note: This example does not consider the application of the constraint on variable consideration (a requirement under Step 3 of the model).



Allocate the transaction price - Exceptions for allocation of a discount

- ❑ An entity is required to allocate a discount entirely to one or more (but not all) performance obligation(s), if all of the following criteria are met:
- ❑ The entity regularly sells each distinct good or service (or each bundle of goods or services) in the contract on a stand-alone basis
- ❑ The entity also regularly sells on a stand-alone basis a bundle (or bundles) of some of those distinct goods or services at a discount
- ❑ The discount (when comparing stand-alone sales of a bundle to stand-alone sales of the distinct goods or services) is substantially the same as the discount in the contract and provides evidence that the entire discount belongs to one (or some) distinct performance obligation(s)

Example

- ❑ An entity enters into a contract with a customer to sell a television, speakers and entertainment unit for a total of INR 21000
- ❑ The television and speakers are delivered at the same time
- ❑ On a regular basis, the entity separately sells the television for INR 17000, the speakers for INR 3000 and the entertainment unit for INR 3000
- ❑ In addition, the entity regularly sells the television and speakers as a bundle for INR 18000
- ❑ The customer purchases all three for INR 21000, receiving a INR 2000 discount for buying the products as a bundle

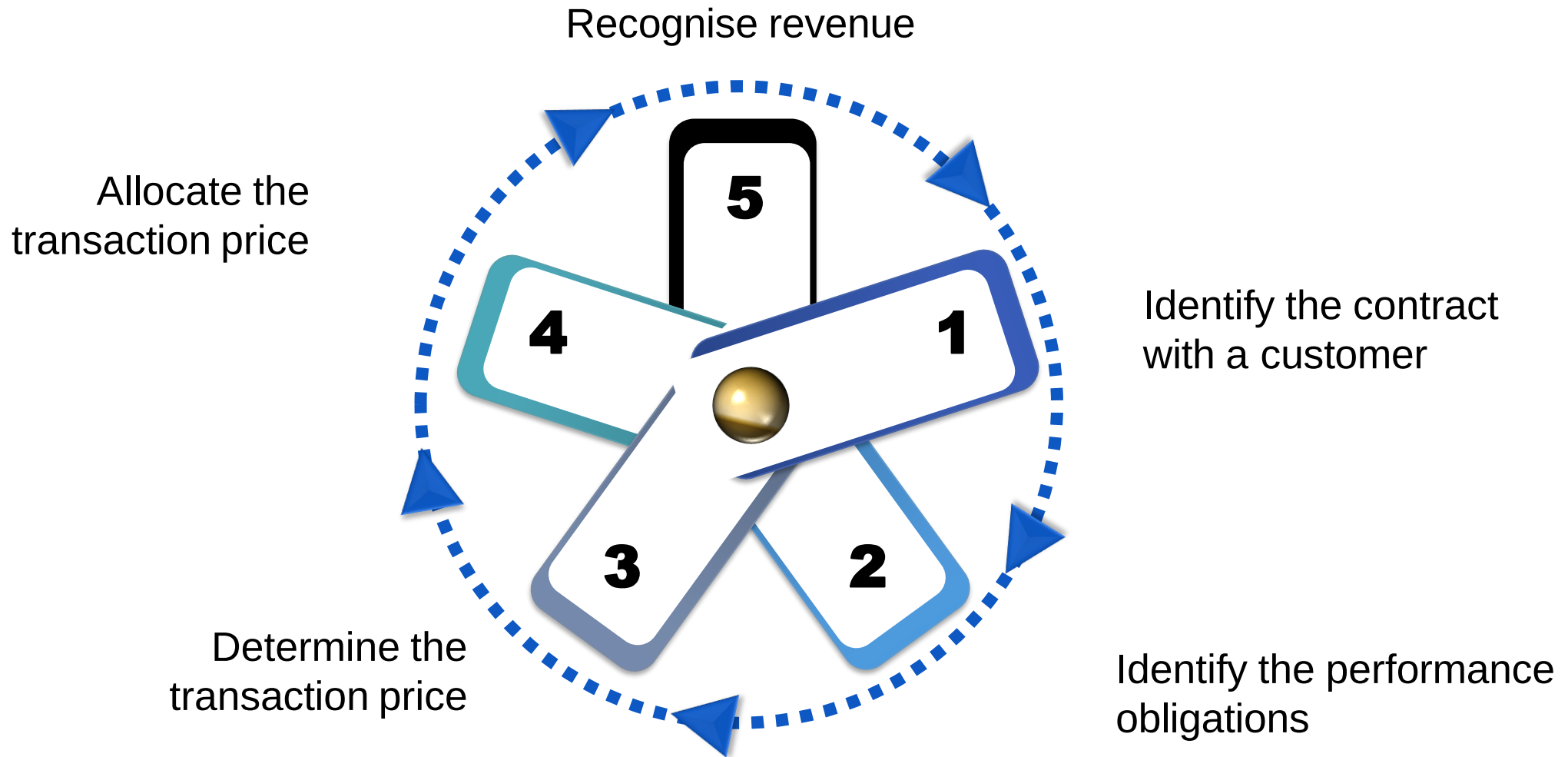


Allocate the transaction price - Exceptions for allocation of a discount

Allocation for the contract

Separate performance obligations	Allocated amounts
Television and speakers (sold as a bundle)	1,8000
Entertainment unit	3000
Total	21000

The Five Step Model Overview



Recognise Revenue as Performance Obligations Satisfied

An performance obligation is satisfied over time if either:

1

Customer simultaneously receives and consumes the benefits as the entity performs.

Routine or
recurring
services.

2

The customers controls the asset as the entity creates or enhances it.

Asset built on
customer's site.

3

The entity's performance does not create an asset for which the entity has an alternate use and there is a right to payment for performance to date.

Asset built to
order.

- Entity agrees to build a specialised equipment to integrate with the customer's existing plant.
- Customer can cancel contract on 30 days notice.
- If the contract is cancelled the entity has a right to payment that covers costs incurred.
- Customer has agreed to make quarterly payments.

Q: Do the terms meet the no alternate use and right to payment criteria?

No alternate use



Right to payment



- Payment needs to approximate selling price of goods and services transferred to date – i.e. payment amount should include a profit margin.

For each performance obligation an entity chooses the method that best depicts performance.

Output method

- Surveys
- Milestones reached
- Units delivered

Input method

- Costs incurred
- Labour hours
- Machine hours

- ❑ Units delivered and similar methods not appropriate if work in progress is material.
- ❑ Adjustments required for wastage and uninstalled materials when cost method used.

Transfer of control at a point in time when customer has...

A present
obligation to
pay

Legal title

Physical
possession

Risks and
rewards of
ownership

Accepted the
asset

Exception: Separate requirements for distinct licences of intellectual property.



Recognise revenue as performance obligations are satisfied

Example

- ☐ Software entity enters into a contract with a customer to:
 - ☐ License software that it delivers immediately
 - ☐ Provides basic installation services that does not significantly alter the software and subsequent telephone assistance
- ☐ Software entity determines the following:
 - ☐ The performance obligations are distinct
 - ☐ The software licence (delivered immediately after contract is finalised) was transferred and is complete (assume for this example the entity determines the licence provides a right to use the intellectual property as it exists at a point in time)
 - ☐ The installation services are recognised on completion of installation
 - ☐ The telephone assistance services are recognised over a period of time

Example

- ☐ A sale subject to an entity's unconditional obligation or right to repurchase the asset (a forward or a call option) would not be considered a sale under the new standard
- ☐ Treated as a lease if repurchase price is lower than original sales price
- ☐ Treated as a financing arrangement if repurchase price is greater than or equal to original sales price
- ☐ A customer's right to require the entity to repurchase the asset (put option) would be outside the scope of the new standard if the customer has significant economic incentive to exercise that right
- ☐ If such an incentive exists, the transaction is accounted for as a lease
- ☐ If such an incentive does not exist, the transaction is accounted for as a sale with a right of return
- ☐ Manufacturer of scissor-lift equipment (scissor lifts) enters into an agreement to sell six scissor lifts
- ☐ The agreement includes an unconditional obligation of the manufacturer to repurchase the scissor-lift equipment from the customer in three years for 70% of the original purchase price (in substance a forward contract)

Solution

- ☐ Since the obligation is to repurchase the asset at a price lower than the original purchase price, the transaction is accounted for as a lease

The image shows a high-angle view of a modern office interior with large glass windows. Three people are silhouetted against the bright light coming from the windows. They are standing on a polished floor that reflects their forms. The view outside the windows shows a cityscape with buildings and greenery under a sky with large, white clouds. The overall mood is professional and contemplative.

Contract Costs

Contract Costs

Costs to obtain a contract

Capitalise incremental costs if:

✓ Incurred only as result of obtaining the contract

✓ Recovery is expected

e.g. sales commission

Costs to fulfil a contract

Capitalise fulfilment costs if:

✓ Directly related

✓ Generate or enhance resources

✓ Recovery is expected

Practical expedient

Amortisation period < 1 year?

Expense costs as incurred

Costs to Fulfil a Contract

Direct costs that are eligible for capitalisation if other criteria are met



Direct labour (e.g. employee wages)

Direct materials (e.g. supplies)

Allocation of costs that relate directly to the contract (e.g. depreciation and amortisation)

Cost that are explicitly chargeable to the customer under the contract

Other costs that were incurred only because the entity entered into the contract (e.g., subcontractor costs)

Costs to be expensed when incurred



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

Costs that do not clearly relate to unsatisfied performance obligations

Amortisation and Impairment

Amortisation period

Systematic basis consistent with the pattern of transfer

Considers anticipated contracts (e.g. renewal options)

Impairment loss recognised to the extent that the carrying amount exceeds:

Remaining amount of consideration expected to be received



Costs directly related to providing goods or services

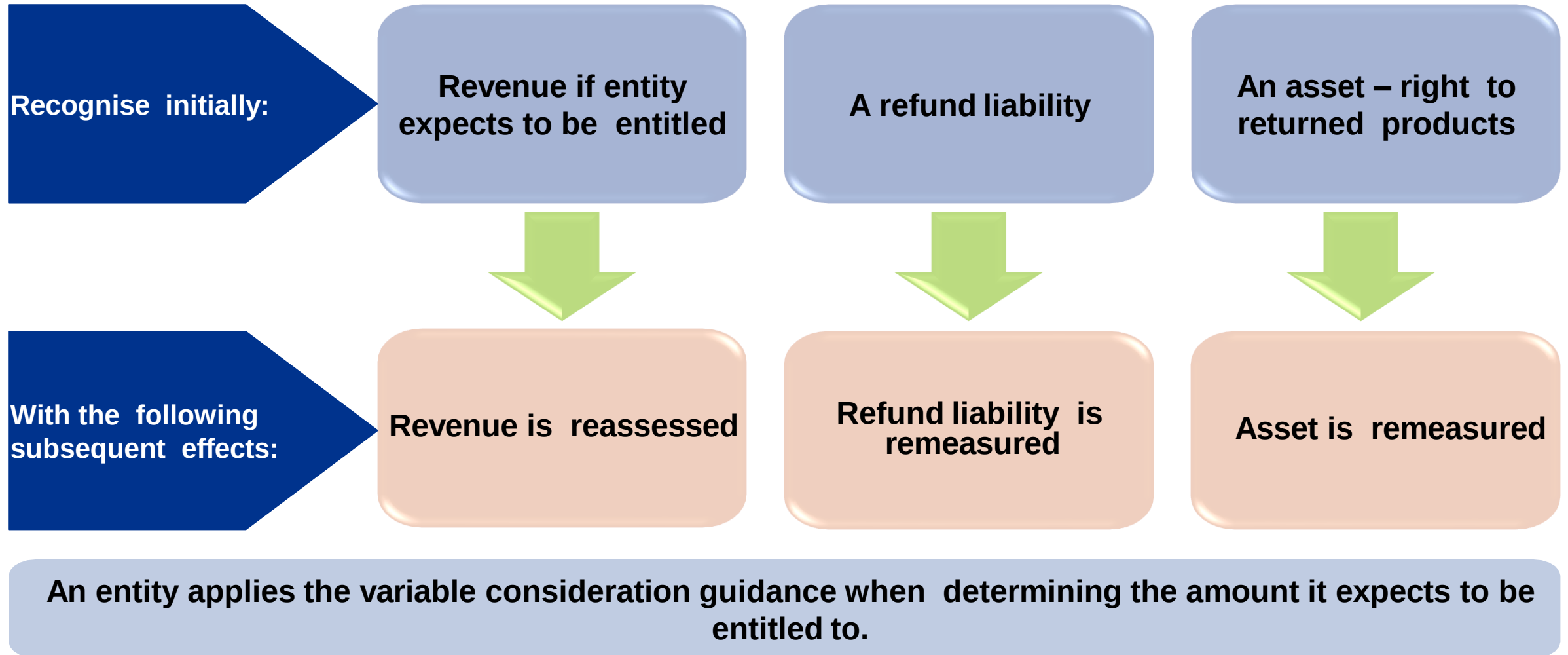
Reversals of impairment

When conditions improved



Application Guidance

Sales with a Right of Return



Sales with a Right of Return

- Company B sells 50 tablet devices @ INR200 each, total INR10,000.
- Return undamaged device within 30 days for a full cash refund.
- Cost of each device is INR150.
- Based on its past experience, B estimates that 3 tablets will be returned (most likely approach).

Q: What entries should B record on transfer of the products?

	Debit	Credit
Cash (or receivable)	10,000	
Refund liability (INR200 x 3 tablets to be returned) Revenue		600
		9,400
Asset (INR150 x 3 tablets to be returned)	450	
Cost of sales Inventory	7,050	
		7,500



Gross presentation

- Allowance for returns is presented gross:
 - as a refund liability; and
 - an asset for recovery of transferred goods.



End result is broadly similar in practice

- New judgements required for estimating variable consideration and applying the constraint.
- Portfolio level estimates may be required.



Determine the transaction price - Variable consideration - rights of return

- ☐ Rights of return are a form of variable consideration
- ☐ Revenue recognition is limited to amounts for which it is 'highly probable' a significant reversal will not occur (i.e., it is highly probable the goods will not be returned)
- ☐ A refund liability is established for the expected amount of refunds and credits to be issued to customers
- ☐ Corresponding asset and adjustment to cost of sales is recorded for items expected to be returned, based on carrying amount of the asset transferred less costs to recover
- ☐ Return assets must be recorded separately from inventory
- ☐ Return assets are subject to impairment testing

Example

- ❑ Game Co sells 1,000 video games to Distributor for INR 50 each.

Distributor has the right to return the video games for a full refund for any reason within 180 days of purchase.

- ❑ The cost of each game is INR 10.
- ❑ Game Co estimates, based on the expected value method, that 6% of sales of the video games will be returned and it is highly probable that returns will not be higher than 6%.
- ❑ Game Co has no further obligations after transferring control of the video games.

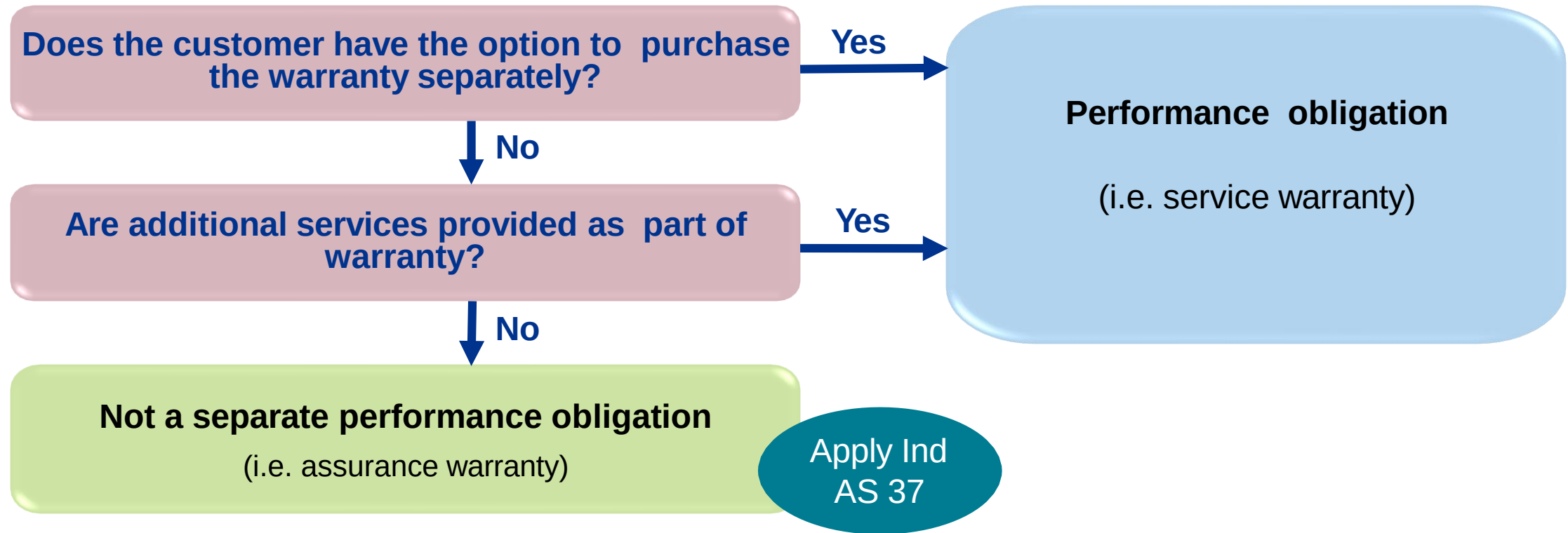
How should Game Co record this transaction?

Sales with a Right of Return

Entry	Dr.	Cr.
Bank (1,000x50)	50,000	
Revenue (940x50)		47,000
Liability (60x50)		3,000
Cost of Sales (940x10)	9,400	
Other assets (60x10)	600	
Inventory (1,000x10)		10,000

- ☐ The return asset will be presented and assessed for impairment separately from the refund liability.
- ☐ Game Co will need to assess the return asset for impairment, and adjust the value of the asset if it becomes impaired.

Warranties



Factors to consider whether a warranty provides an additional service:

Is it required by law?

Is it longer than customary?

What tasks are performed?

Warranties

- Car manufacturer N sells to customer A:



Car



Standard warranty: 3
years or 36,000 KM

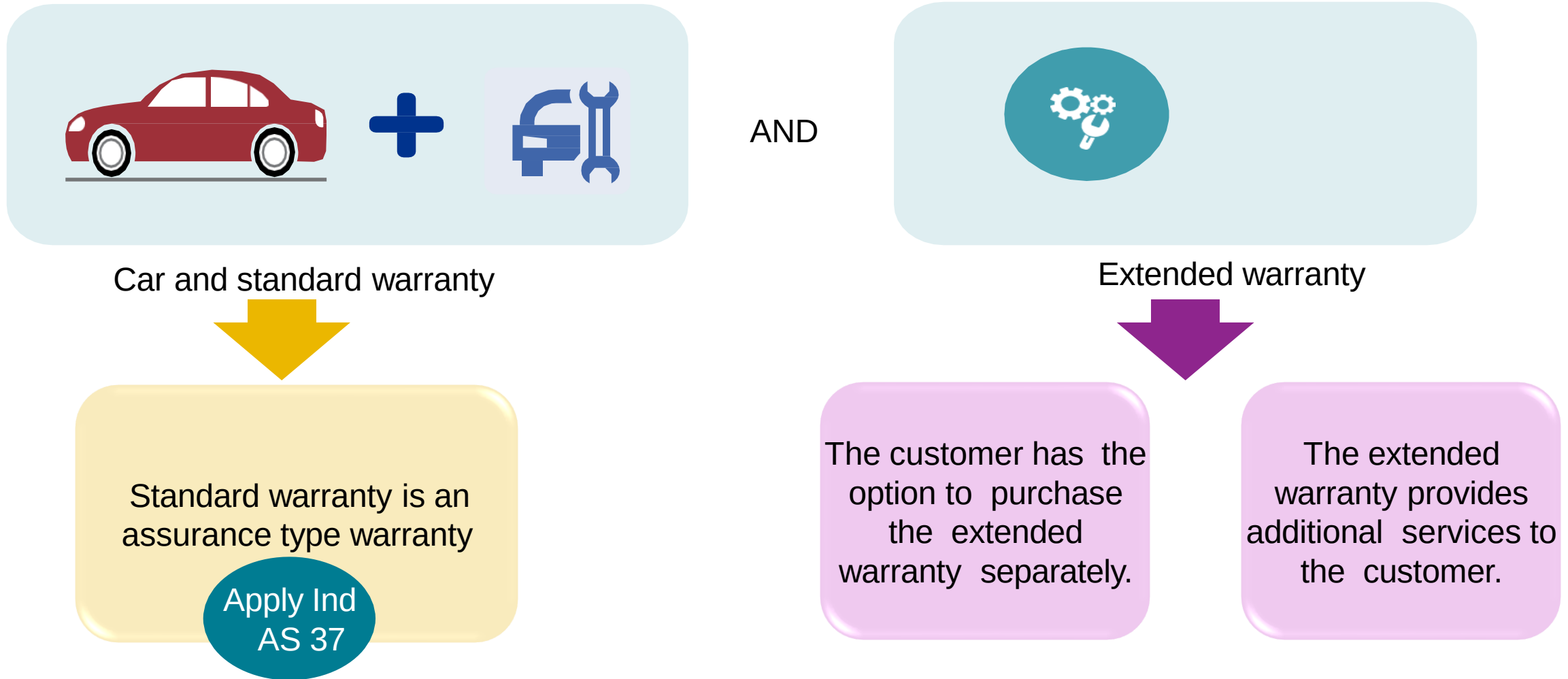


Extended warranty: additional
3 years or up to 70,000 miles
for INR5,000

Q: How many performance obligations are there in the contract?

Performance Obligations

Performance obligations:





'Service' warranties accounted for as a performance obligation

- Rather than evaluating whether risks and rewards of ownership have passed to the buyer, assess whether additional services are provided.
- Presence of a warranty does not preclude revenue recognition.



Revenue recognition may be accelerated

- Allocation of the transaction price to a performance obligation.

Principal versus Agent

If the entity obtains control of a promised good or service in advance of transferring the good or service to a customer

Then

The entity is principal in the transaction

Revenue recognised gross

Another party is primarily responsible for fulfilling the contract

The entity does not have discretion in establishing prices

The entity does not have inventory risk

The entity's consideration is in the form of a commission

The entity is not exposed to credit risk

Indicators that the entity is agent in the transaction

Revenue recognised net

Customer options for additional goods or services

e.g. sales incentives, loyalty points, contract renewal options

Does the option provide a *material right* the customer would otherwise not receive?

Yes – account for as a performance obligation. Revenue recognised when future goods or services transferred or option expires.

Customers' unexercised rights (breakage)

e.g. gift vouchers, non-refundable tickets

Expect to be entitled to breakage amount?

Yes – recognise breakage amount as revenue in proportion to pattern of rights exercised.

No – recognise as revenue when likelihood of customer exercise becomes remote.

Application Guidance: Other Topics

Non-refundable upfront fees

e.g. joining fees, activation fees, setup fees

Does the fee result in the transfer of a promised good or service?

If not – advance payment for future goods or services. Revenue recognised when those goods or services are provided.

Consignment arrangements

e.g. delivery to a dealer or distributor prior to sale end to customer

Is delivered inventory controlled by the entity? (e.g. control not transferred until sale or expiry of a specified period)

If so – revenue is not recognised on delivery of the products to the intermediary.

Bill and hold arrangements

i.e. entity bills customer but retains physical possession

Consider whether:

- the reason for arrangement is substantive;
- the product is separately identified;
- the product is ready for physical transfer; and
- the entity has the ability to use the product or direct it to another customer.

Customer acceptance

e.g. trial period, cancellation clauses or remedial action that can be taken by a customer

Can the entity objectively determine that control of a good or service has been transferred in accordance with the contract?

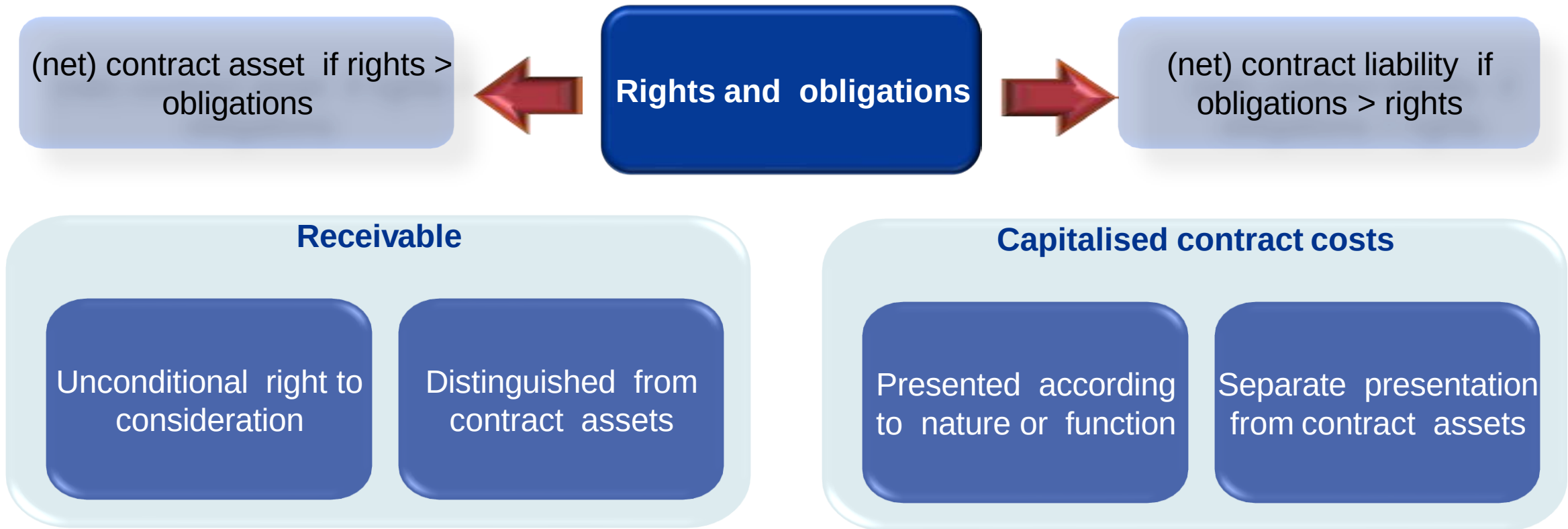
Consider the entity's experience with similar contracts; remaining performance obligations.



Presentation and Disclosures

Contract asset or contract liability is recognised when the:

- entity performs by transferring goods or services; or
- customer performs by paying consideration to entity.



Disclosure

Objective: help users understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers

Contracts with customers

Significant judgements and changes in judgements

Disaggregation of revenue

Determining the timing of satisfaction of performance obligations

Changes in contract assets, liabilities and costs

Determining the transaction price

Performance obligations

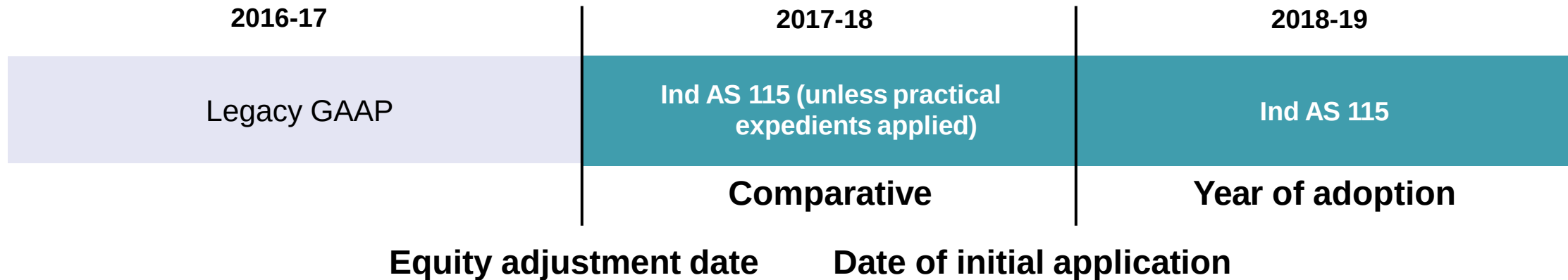
Determining amounts allocated to performance obligations

Assets recognised from the costs to obtain or fulfil a contract

A group of people are kayaking on a calm lake during sunset. The kayakers are in yellow kayaks, and the sun is low on the horizon, creating a warm, golden glow. The water is dark, and the sky is a mix of blue and orange. The kayakers are in motion, with splashes of water visible around their kayaks. The background features a line of trees and distant mountains.

Effective Date and Transition

Transition – first time adoption



- A first-time adopter is not required to restate contracts that were completed before the earliest period presented. (A completed contract is a contract for which the entity has transferred all of the goods or services identified in accordance with previous GAAP)
- A first-time adopter may use certain specified practical expedients when applying Ind AS 115 retrospectively (eg. for completed contracts, an entity need not restate contracts that begin and end within the same annual reporting period)

Key Facts – Notable Differences from Current Requirements

Current guidance

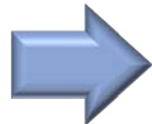
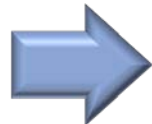
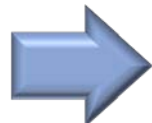
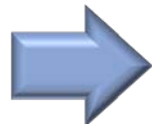
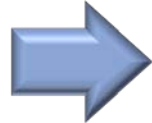
Guidance contained in multiple standards and interpretations

Risk and rewards based model

Revenue is recognised mainly considering the form of the contract.

No specific guidance on identifying performance obligations in a contract.

Revenue is recognised at the contractual value of the consideration



New standard

All guidance contained in a single standard

Control based model. Risk and rewards is retained as indicator of control transfer for performance obligations satisfied at a point in time.

Revenue is recognised considering the substance of the contract.

Specific guidance on identifying performance obligations in a contract.

Revenue is recognised at the amount of the consideration to which an entity expects to be entitled.

Key Facts – Notable Differences from Current Requirements

Current guidance

Does not provide guidance on combining contracts (except for construction contracts). Currently, revenue is mainly recognised based on the legal form of the contract and at prices stated therein.

No explicit guidance for gross versus net reporting of revenue exists and practice in this area varies.

Limited/no guidance on specific areas like barter, loyalty programmes, costs to obtain a contract, licences etc

Limited disclosure requirements.



New standard

Explicit guidance on combining of contracts.

The requirement of gross versus net reporting is driven by an assessment of principle versus agent relationship.

Specific guidance on these areas to enable consistency in practice.

Several qualitative and quantitative disclosures required.



Key Impact

Key impact

- ☐ Change of model from risk and rewards to control
- ☐ Multiple element contracts
- ☐ New concept of performance obligations including whether customer receives a stand-alone benefit
- ☐ Revenue recognition at a point in time v overtime
- ☐ Principal v agent
- ☐ Licences
- ☐ Warranties
- ☐ Sales return
- ☐ Variable consideration in the contract
- ☐ Consideration paid to customer
- ☐ Non-cash consideration
- ☐ Separation of financing component
- ☐ Contracts that are not enforceable, including where customer is unable to pay
- ☐ Volume discounts and other material rights provided to customers
- ☐ Bill and hold arrangements
- ☐ Sale and Repurchase agreements
- ☐ Contract costs; and
- ☐ Contract modification



Ind AS 114 Regulatory Deferral Accounts

Objective and Scope

Objective.

The objective of Ind-AS 114 is to specify the financial reporting requirements for 'regulatory deferral account balances' that arise when an entity provides good or services to customers at a price or rate that is subject to rate regulation.

Scope.

Ind-AS 114 is permitted, but not required, to be applied where an entity conducts rate-regulated activities and has recognised amounts in its previous GAAP financial statements that meet the definition of 'regulatory deferral account balances' (sometimes referred to 'regulatory assets' and 'regulatory liabilities').

When applied, the requirements of Ind-AS 114 must be applied to all regulatory deferral account balances arising from an entity's rate-regulated activities.

Explanation: Guidance Note on Accounting for the Rate Regulated Activities, issued by the Institute of Chartered Accountants of India (ICAI) shall be considered to be the **previous GAAP**.

Rate regulation

A framework for establishing the prices that can be charged to customers for goods and services and that framework is subject to oversight and/or approval by a rate-regulator

Rate regulator

An authorised body that is empowered by statute or regulation to establish the rate or range of rates that bind an entity. The rate regulator may be a third-party body or a related party of the entity, including the entity's own governing board, if that body is required by statute or regulation to set rates both in the interest of customers and to ensure the overall financial viability of the entity

Regulatory deferral account balance

The balance of any expense (or income) account that would not be recognised as an asset or a liability in accordance with other Standards, but that qualifies for deferral because it is included, or is expected to be included, by the rate regulator in establishing the rate(s) that can be charged to customers

Accounting policies for regulatory deferral account balances

- ❑ Ind-AS 114 provides an exemption from paragraph 11 of Ind-AS 8 Accounting Policies, Changes in Accounting Estimates and Errors when an entity determines its accounting policies for regulatory deferral account balances. Paragraph 11 of Ind-AS 8 requires an entity to consider the requirements of Ind-ASs dealing with similar matters and the requirements of the Conceptual Framework when setting its accounting policies.
- ❑ The effect of the exemption is that eligible entities can continue to apply the accounting policies used for regulatory deferral account balances under the basis of accounting used immediately before adopting Ind-AS 10 ('previous GAAP') when applying Ind-AS 10 s, subject to the presentation requirements of Ind-AS 114 .
- ❑ Entities are permitted to change their accounting policies for regulatory deferral account balances in accordance with Ind-AS 8, but only if the change makes the financial statements more relevant and no less reliable, or more reliable and not less relevant, to the economic decision-making needs of users of the entity's financial statements. However, an entity is not permitted to change accounting policies to start to recognise regulatory deferral account balances.

Interaction with other Standards

Ind-ASs	Applicability/ Exemptions.
Ind-AS 10 Events After the Reporting Period	The requirements of Ind-AS 10 are applied when determining which events after the end of the reporting period should be taken into account in the recognition and measurement of regulatory deferral account balances
Ind-AS 12 Income Taxes	Deferred tax assets and liabilities arising from regulatory deferral account balances are presented separately from total deferred tax amounts and movements in those deferred tax balances are presented separately from tax expense (income)
Ind-AS 33 Earnings Per Share	Entities applying Ind-AS 114 are required to present an additional basic and diluted earnings per share that excludes the impacts of the net movement in regulatory deferral account balances
Ind-AS 36 Impairment of Assets	Regulatory deferral account balances are included in the carrying amount of any relevant cash-generating unit (CGU) and are treated in the same way as other assets and liabilities where an impairment loss arises
Ind-AS 103 Business Combinations	The entity's accounting policies for regulatory deferral account balances are used in applying the acquisition method, which can result in the recognition of regulatory deferral account balances in respect of an acquiree, regardless of whether the acquiree itself recognised such balances
Ind-AS 105 Non-current Assets Held for Sale and Discontinued Operations	The measurement requirements of Ind-AS 105 do not apply to regulatory deferral account balances, and modifications are made to the presentation of information about discontinued operations and disposal groups in relation to such balances
Ind-AS 110 Consolidated Financial Statements and Ind-AS 28 Investments in Associates and Joint Ventures	The entity's accounting policies in respect of regulatory deferral account balances are required to be applied in an entity's consolidated financial statements or in the determination of equity accounted information of associates or joint ventures, notwithstanding that the entity's investees may not have recognised regulatory deferral account balances in their financial statements
Ind-AS 112 Disclosure of Interests in Other Entities	Separate disclosure of regulatory deferral account balances and net movements in those balances recognised in profit or loss or other comprehensive income are required for various Ind-AS 112 disclosures

The impact of regulatory deferral account balances are separately presented in an entity's financial statements. This requirements applies regardless of the entity's previous presentation policies in respect of regulatory deferral balance accounts under its previous GAAP. Accordingly:

- ❑ Separate line items are presented in the statement of financial position for the total of all regulatory deferral account debit balances, and all regulatory deferral account credit balances.
- ❑ Regulatory deferral account balances are not classified between current and non-current, but are separately disclosed using subtotals.
- ❑ The net movement in regulatory deferral account balances are separately presented in the other comprehensive income section of statement of profit or loss using subtotals.

Ind-AS 114 sets out disclosure objectives to allow users to assess:

- the nature of, and risks associated with, the rate regulation that establishes the price(s) the entity can charge customers for the goods or services it provides - including information about the entity's rate-regulated activities and the rate-setting process, the identity of the rate regulator(s), and the impacts of risks and uncertainties on the recovery or reversal of regulatory deferral balance accounts
- the effects of rate regulation on the entity's financial statements - including the basis on which regulatory deferral account balances are recognised, how they are assessed for recovery, a reconciliation of the carrying amount at the beginning and end of the reporting period, discount rates applicable, income tax impacts and details of balances that are no longer considered recoverable or reversible.



Questions & Answers

THANK YOU

For further information please contact

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