Educational Material on
Ind AS 115, *Revenue from Contracts with Customers*

The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
New Delhi

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Foreword

The financial reporting has always been critical from the point of view of allocation of economic resources. Meaningful and transparent financial reporting serves an entity favourably in the long run since it establishes the credibility of an entity in the eyes of the investors, regulators and other users. Further, information about a particular entity is greatly useful if it can be compared with similar information about another entity. Comparability between entities and consistency in the application of methods over time increases the informational value of comparisons of relative economic opportunities or performance. In this era of globalisation, to address this issue of comparability across the globe and considering other factors, need for a single set of high quality accounting standards has been felt. This need has been taken care by the International Accounting Standards Board (IASB) by issuing International Financial Reporting Standards (IFRSs) which are increasingly being recognised as Global Financial Reporting Standards.

Keeping this in view, India has also decided to converge with IFRS. For this purpose, the Institute of Chartered Accountants of India (ICAI) is actively engaged in formulation of IFRS-converged Indian Accounting Standards (Ind ASs). Another very significant responsibility of the ICAI is getting the members and other stakeholders ready for proper implementation of these Standards, which is being discharged by the ICAI through its Ind AS Implementation Group. To accomplish its primary objective of providing guidance to members and other stakeholders for implementation of Ind AS, the Group formulates Educational Materials on Ind ASs.

An Educational Material contains summary of the respective Indian Accounting Standard and Frequently Asked Questions (FAQs) covering the issues which are expected to be encountered frequently while implementing the Standard. Accordingly, the Group has come out with the Educational Material on Ind AS 115, *Revenue from Contracts with Customers*.

I acknowledge the sincere efforts of CA. Nihar Niranjan Jambusaria, Convenor, Ind AS Implementation Group and CA. Dhinal Ashvinbhai Shah, Deputy Convenor, and all the members of the Ind AS Implementation Group for bringing out this Educational Material on an Indian Accounting Standard which deals with a very important aspect of the financial statements, i.e., revenue. I also congratulate CA. S. B. Zaware, Chairman and CA. M. P. Vijay Kumar, Vice-chairman of Accounting Standards Board of ICAI for their support. Since the subject is relevant for all the entities, I am confident that this Educational Material will be very useful for the members of the Institute and other concerned stakeholders in proper understanding and implementation of the Standard.

New Delhi | **CA. Naveen N.D. Gupta**
August 02, 2018 | ***President, ICAI***

Preface

In the era of globalised economies, Ind AS is a business imperative for Indian companies today. Ind AS converged with IFRS have put India at the centre stage of high quality and transparent financial reporting whose benefits far outweigh the challenges. These standards will facilitate better comparability and understanding of financial statements across all companies around the world and are the new benchmark of accounting excellence. In India, Ind AS has become a reality now as the era of Implementation of Ind AS has already begun in the country with Phase I companies which have published their financial statements prepared in accordance with Ind AS for financial year 2016-17. Phase II companies have also started publishing their financial statements in accordance with Ind AS.

The Institute of Chartered Accountants of India (ICAI) through its Ind AS Implementation Group is making every possible effort to ensure that these Standards are implemented in the same spirit in which these have been formulated. For this purpose, the Group is working to provide guidance to the members and other stakeholders by issuing Educational Materials on Ind AS, issuing timely clarifications on issues being faced by the members through Ind AS Technical Facilitation Group (ITFG) Clarification Bulletins, addressing queries through Support-desk for implementation of Ind AS, conducting Certificate Course on Ind AS, developing e-learning modules on Ind AS, workshops, seminars, awareness programmes on Ind AS and series of webcasts on Ind AS etc.

We are glad that the Group has brought out the Educational Material on Indian Accounting Standard (Ind AS) 115, *Revenue from Contracts with Customers*. The objective of Ind AS 115 is to establish the principles that an entity shall apply to report useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer. The core principle of Ind AS 115 is that an entity recognises 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. This Educational Material contains summary of Ind AS 115 discussing the key requirements of the Standard and the Frequently Asked Questions

(FAQs) covering the issues, which are expected to be encountered frequently while implementing this Standard.

We may mention that the views expressed in this publication are the views of the Ind AS Implementation Group and are not necessarily the views of the Council of the Institute. The purpose of this publication is to provide guidance for implementing this Ind AS effectively by explaining the principles enunciated in the Standard with the help of examples. However, while applying Ind AS in a practical situation, reference should be made to the full text of the Standards.

We would like to convey sincere gratitude to our Hon'ble President, CA. Naveen N D Gupta and Vice-President, CA. Prafulla Premsukh Chhajed for providing us this opportunity of bringing out implementation guidance on Ind AS in the form of Educational Materials. We sincerely appreciate the efforts put in by Co-convenor and members of the Group, CA. Sandip Khetan, CA. Archana Bhutani, CA. Anand Banka, CA. Gargi Ray, CA. Gopalakrishnan R, CA. Rohit Kumar Agarwala, CA. Sujit Mahato, CA Parveen Kumar, CA. M.M. Kawatra and CA. Mayur Gupta for preparing the draft of this Educational Material. We would also like to thank all the members of the Ind AS Implementation Group for their valuable & technical contributions in finalising this publication.

We sincerely appreciate CA. Geetanshu Bansal, Secretary, Ind AS Implementation Group and CA. Prachi Jain, Executive Officer for their technical and administrative support in bringing out this publication. We would also like to thank CA. Vidhyadhar Kulkarni, Head, Technical Directorate, for his guidance.

We are sure that this Educational Material will be of great help in understanding the provisions of Ind AS 115 and in their practical implementation.

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Convenor
Ind AS Implementation Group

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Deputy Convenor
Ind AS Implementation Group

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Educational Material on Indian Accounting Standard (Ind AS) 115 *Revenue from Contracts with Customers*

I. Summary

Objective

This standard establishes principles to report useful information about the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer.

The core principle is that an entity shall recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

The standard specifies the accounting for an individual contract with a customer. However, as a practical expedient, an entity may apply this Standard to a portfolio of contracts (or performance obligations) with similar characteristics if the entity reasonably expects that the effects of applying the Standard to the portfolio would not differ materially from applying this Standard to the individual contracts (or performance obligations) within that portfolio.

Scope

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

(a) lease contracts within the scope of Ind AS 17, *Leases*;

(b) insurance contracts within the scope of Ind AS 104, *Insurance Contracts*;

(c) financial instruments and other contractual rights or obligations within the scope of Ind AS 109, *Financial Instruments*, Ind AS 110, *Consolidated Financial Statements*, Ind AS 111, *Joint Arrangements*, Ind AS 27, *Separate Financial Statements* and Ind AS 28, *Investments in Associates and Joint Ventures*; and

(d) non-monetary exchanges between entities in the same line of business to facilitate sales to customers or potential customers. For example, this Standard would not apply to a contract between two oil companies that agree to an exchange of oil to fulfil demand from their customers in different specified locations on a timely basis.

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

A **customer** is a party that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration.

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

Recognition

Identifying the contract

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

(a) the parties to the contract have approved the contract (in writing, orally or in accordance with other customary business practices) and are committed to perform their respective obligations;

(b) the entity can identify each party's rights regarding the goods or services to be transferred;

(c) the entity can identify the payment terms for the goods or services to be transferred;

(d) the contract has commercial substance (ie the risk, timing or amount of the entity's future cash flows is expected to change as a result of the contract); and

(e) it is probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. In evaluating whether collectability of an amount of consideration is probable, an entity shall consider only the customer's ability and intention to pay that amount of consideration when it is due. The amount of consideration to which the entity will be entitled may be less than the price stated in the contract if the consideration is variable because the entity may offer the customer a price concession.

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

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

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

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

(b) the contract has been terminated and the consideration received from the customer is non-refundable.

Contract modification

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

(a) the scope of the contract increases because of the addition of promised goods or services that are distinct; and

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

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

(a) account for as if it were a termination of the existing contract and the creation of a new contract, if the remaining goods or services are distinct from the goods or services transferred. The amount of consideration to be allocated is the sum of:

  (i) the consideration promised by the customer (including amounts already received from the customer) that was included in the estimate of the transaction price and that had not been recognised as revenue; and

  (ii) the consideration promised as part of the contract modification.

(b) account for as if it were a part of the existing contract if the remaining goods or services are not distinct and, therefore, form part of a single performance obligation that is partially satisfied at the date of the contract modification.

(c) If the remaining goods or services are a combination of items (a) and (b), then the effects of the modification on the unsatisfied (including partially unsatisfied) performance obligations in the modified contract shall be accounted for in a manner that is consistent with the objectives of this paragraph.

Identifying performance obligations

At contract inception, assess the goods or services promised and identify as a performance obligation each promise to transfer to the customer either:

(a) a good or service (or a bundle of goods or services) that is distinct; or

(b) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.

Distinct goods or services

A good or service is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (i.e. the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (i.e. the promise to transfer the good or service is distinct within the context of the contract).

Satisfaction of performance obligations

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

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

Performance obligations satisfied over time

A performance obligation is satisfied over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs;

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced; or

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

For some types of performance obligations, assessment of (a) above would be straightforward. For other types, entity may not be able to readily identify whether a customer simultaneously receives and consumes the benefits from the entity's performance as the entity performs. In those circumstances, a performance obligation is satisfied over time if an entity determines that another entity would not need to substantially re-perform the work that the entity has completed to date if that other entity were to fulfil the remaining performance obligation to the customer.

In assessing whether an asset has an alternative use to an entity, an entity shall consider the effects of contractual restrictions and practical limitations on the entity's ability to readily direct that asset for another use, such as selling it to a different customer. A contractual restriction must be substantive i.e. a customer could enforce its rights to the promised asset if the entity sought to direct the asset for another use.

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

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

Output methods recognise revenue on the basis of direct measurements of the value to the customer of the goods or services transferred to date relative to the remaining goods or services promised under the contract.

Input methods recognise revenue on the basis of the entity's efforts or inputs to the satisfaction of a performance obligation (for example, resources consumed, labour hours expended, costs incurred, time elapsed or machine hours used) relative to the total expected inputs to the satisfaction of that performance obligation.

Measurement

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

Determining the transaction price

Entity shall consider the terms of the contract and its customary business practices to determine the transaction price. The transaction price is the amount that the entity expects to be entitled to in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties (for example, some sales taxes). The consideration promised may include fixed amounts, variable amounts, or both.

Variable consideration

If the consideration promised in a contract includes a variable amount, an entity shall estimate the amount of consideration to which the entity will be entitled in exchange for transferring the promised goods or services to a customer.

Estimate amount of variable consideration by using either of the following methods:

- The expected value—the expected value is the sum of probability-weighted amounts in a range of possible consideration amounts. An expected value may be an appropriate estimate of the amount of variable consideration if an entity has a large number of contracts with similar characteristics.
- The most likely amount—the most likely amount is the single most likely amount in a range of possible consideration amounts (i.e., the single most likely outcome of the contract). The most likely amount may be an appropriate estimate of the amount of variable consideration if the contract has only two possible outcomes (for example, an entity either achieves a performance bonus or does not).

At the end of each reporting period, an entity shall update the estimated transaction price including updating its assessment of whether an estimate of variable consideration is constrained.

The existence of a significant financing component in the contract

In determining the transaction price, an entity shall adjust the promised amount of consideration for the effects of the time value of money if the timing of payments agreed to by the parties to the contract (either explicitly or implicitly) provides the customer or the entity with a significant benefit of financing the transfer of goods or services to the customer.