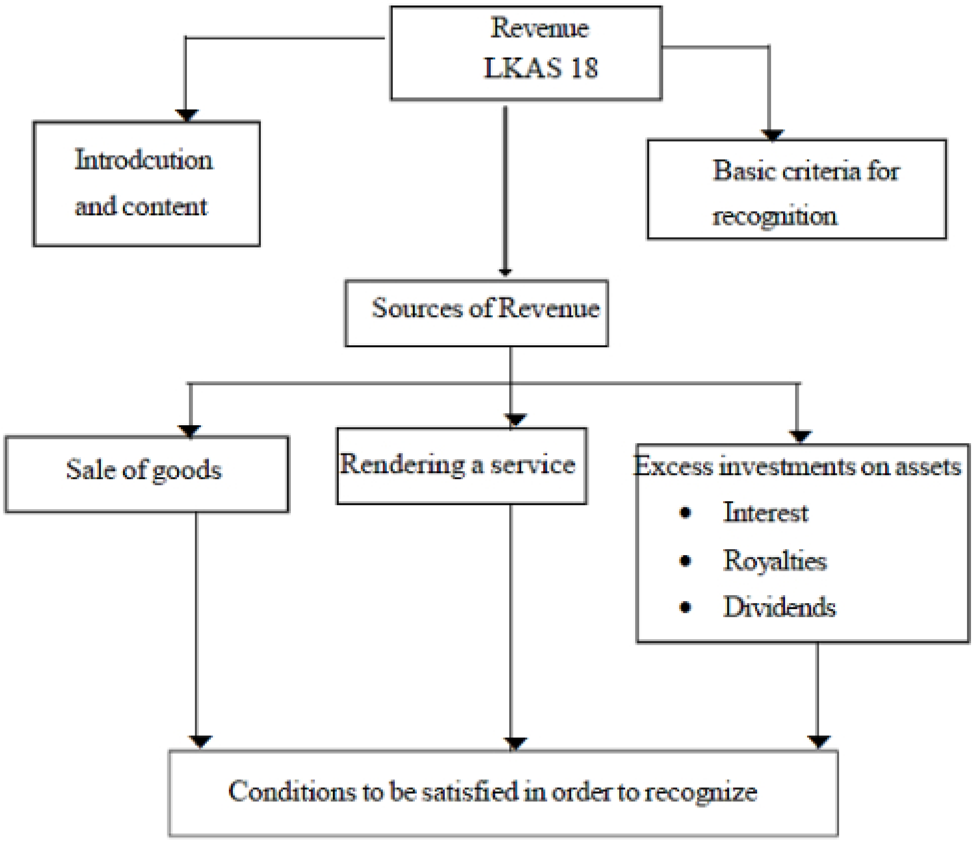
11.9 | Revenues

- **Definition according to the standard**
- **Recognizing a variety of revenues**

Concept map



Revenue

- Revenue arises in ordinary course of activities of an entity. Income can be divided into two:
    - Revenue
    - Profit
- Revenue can be defined as the gross inflow of economic benefits during the period, arising in the course of ordinary activities of an entity, when those inflows result in increases in equity other than increases relating to contributions from equity participants.

Definition for income as per the Framework

- Income is defined as increases in economic benefits during the accounting period in the form of inflows or enhancements of assets, or decreases of liabilities that result increases in equity, other than those relating to contributions from equity participants. Income includes both revenues and gains.

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Revenue as per LKAS 18

Definition for revenue as per LKAS 18:

- Revenue is recognized when it is probable that future economic benefits will flow to the entity and these benefits can be measured reliably.

- According to LKAS 18, the following should be satisfied in order to recognize revenue:
  1. It is probable that economic benefits associated with the transaction will flow to the entity
  2. Amount of revenue can be measured reliably

Example for economic benefits:

Rs. 46 000 cash collected by selling goods, inclusive of 15% VAT, can be divided into two:
1. Sales value of Rs. 40 000 exclusive of VAT (profits earned from that sale is an economic benefit to the organization)
2. VAT amount of Rs. 6 000 collected on behalf of the government does not provide any benefit to the organization

Application of the LKAS 18:

- This standard shall be applied in accounting for revenue arising from the following transactions and events:
  - Sale of goods
  - Rendering of services
  - Use by others of entity assets yielding interest, royalties, and dividends

Disclosures as per LKAS 18:

a) the accounting policies adopted for the recognition of revenue, including the methods adopted to derermine the stage of completion of transactions involving the rendering of services

b) the amount of each significant category of revenue recognized during the period, including revenue arising from:
   1. the sale of goods
   2. the rendering of services
   3. interest
   4. royalties
   5. dividends

c) the amount of revenue arising from exchanges of goods or services included in each significant category of revenue

Sale of goods

- Sale of goods that are produced by the entity for the purpose of sale and goods purchased for resale, could be considered as revenue of an organization.

- Revenue from the sale of goods shall be recognized when all the following conditions have been satisfied:
  a) the entity has transferred to the buyer the significant risks and rewards of ownership of the goods
  b) the entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold
  c) the amount of revenue can be measured reliably
  d) it is probable that the economic benefits associated with the transaction will flow to the entity
  e) the costs incurred or to be incurred in respect of the transaction can be measured reliably

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Rendering of services

- When the outcome of a transaction involving the rendering of services can be estimated reliably, revenue associated with the transaction shall be recognized by reference to the stage of completion of the transaction at the end of the reporting period.

- The outcomes of a transaction can be estimated reliably when all the following conditions are satisfied:
    a) amount of revenue can be measured reliably
    b) it is probable that the economic benefits associated with the transaction will flow to the entity
    c) the stage of completion of the transaction at the end of the reporting period can be measured reliably
    d) the costs incurred for the transaction and the costs to complete the transaction can be measured reliably

Example:
Consultation period of two years given for a project and it will be paid at the end of the service period. Total consultation fee is Rs. 800 000 and at the end of the first year 40% is payable.

The first year 40% payable.

At the end of the first year service income is $800{,}000 \times \frac{40}{100} = Rs.320{,}000$

Interest income

- Interest income is a source of revenue by providing excess resources to other parties.

- Interest income relevant for the period is to be recognized in respect to the time under accrual basis, using the effective interest method.

- Interest income is to be recorded if the amount can be measured reliably and created an inflow of economic benefits.

Example:
On 01.04.2018 an amount of Rs. 500 000 deposited in a fixed investment at an interest rate of 10%. Accounting year ends in on 31.12.2018. Company does not received any interest income during the period. But it can be calculated as follows.

$$500{,}000 \times \frac{10}{100} \times \frac{9}{12} = \text{Rs. } 37\ 500$$

Interest income for the period is Rs. 37 500. It showed be recorded under current asset since they could not collected for the period.

Royalties

- Royalty income should be calculated according to accrual basis.

- It should be recognized as an income only if:
    - it is probable that the economic benefits associated with the transaction will flow to the entity
    - the amount of the revenue can be measured reliably

Example:

An owner of a graphite mine has given authority to extract graphic to another party.

For each tonne of graphite a payments of Rs. 5 000 should be given.

10 tonnes were extracted during the first year and Rs. 40 000 paid each year.

Therefore

Royalty income according to the royalty agreement is Rs. 50 000 calculated based on accrual.

Receivable amount of 10 000 should be shown under current asset.

Dividends

- The amount of dividends payable to each shareholder shall be recognized when the shareholder's right to receive payment is established.

- Dividend income is to be recorded if the amount can be measured reliably and created an inflow of economic benefits.

Example:

Purchased 40 000 shares at a price of Rs. 20 each. It is decided to pay a three dividends to their share holders and obtained approval from the board of directors.

Divided income for the period is Rs. 40 000 shared X 3 each = Rs. 120 000