

AS-9

Revenue Recognition



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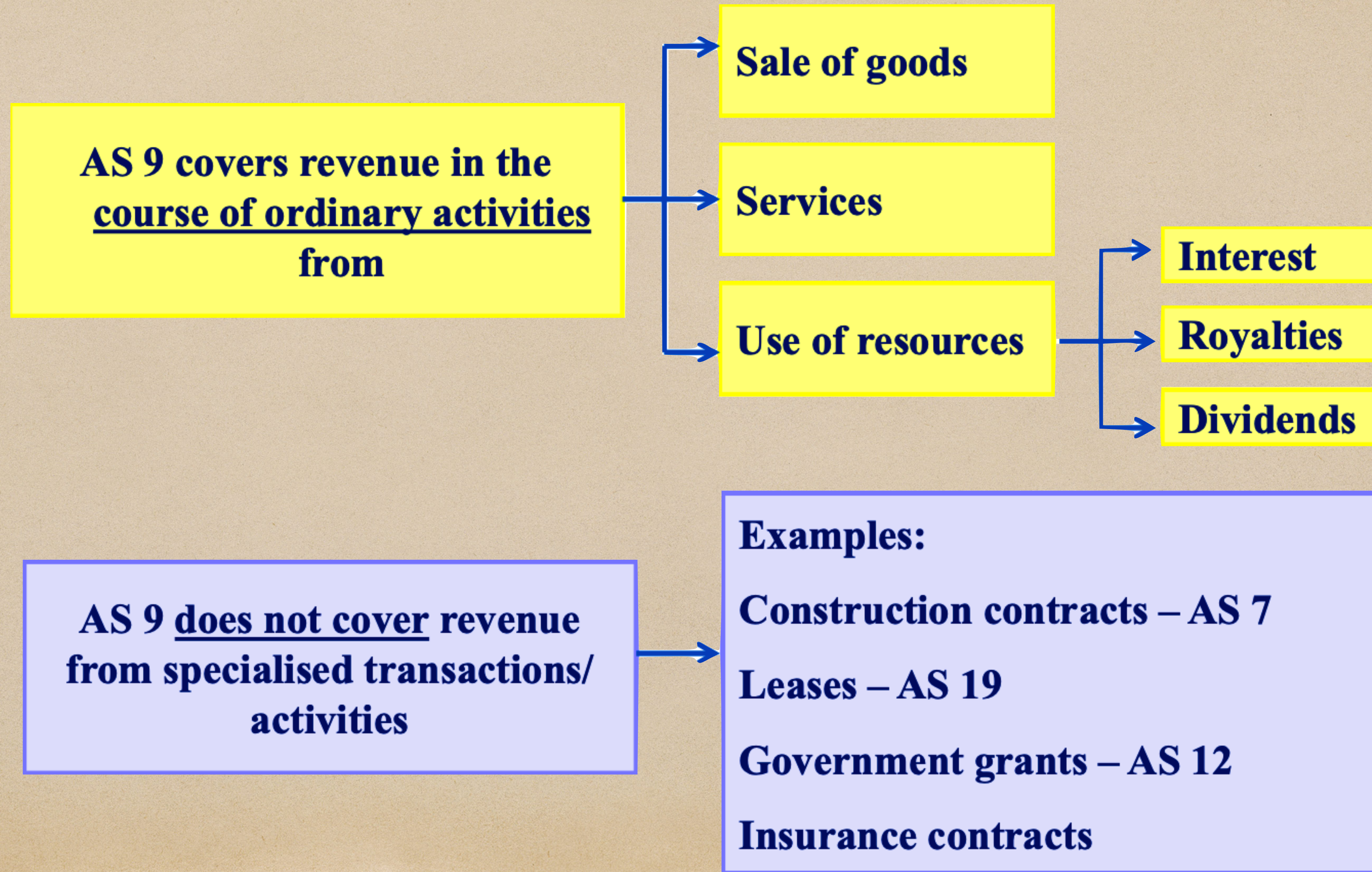
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# When do we need accounting standard 9?





# Definition of Revenue

- Gross inflow of cash, receivables and other considerations
- Arising in the course of ordinary activities
- During the period from sale of goods, rendering of services and from the use by others of enterprise and resources yielding interest, royalty or dividends
- In an agency relationship, revenue is amount of commission and not the gross inflow example sale of airline tickets by a airline agent



## Explanation

Revenue recognition is mainly concerned with the **timing of recognition of revenue** in the statement of profit and loss of an enterprise. The amount of revenue arising on a transaction is usually determined by agreement between the parties involved in the transaction. When uncertainties exist regarding the determination of the amount, or its associated costs, these uncertainties may influence the timing of revenue



# Revenue recognition in sale of goods

Revenue from sale transaction is recognised when the following conditions are satisfied.

## Basic Conditions:

- Property in goods is transferred from seller of goods to the buyer for a price.
- All significant risk and reward of ownership have been transferred to buyer and seller retains no effective control.
- No significant uncertainties exist regarding amount of consideration derived from the sale of goods.

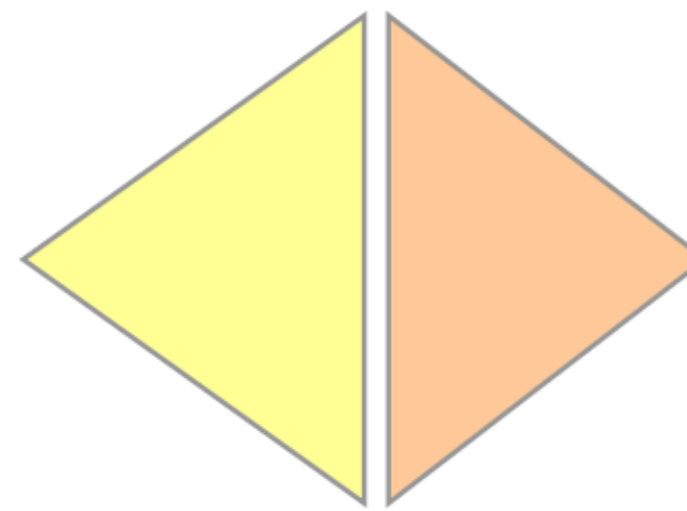


# Revenue recognition in case of Rendering of services

**Performance: Work accomplished should be related to revenue**

## Proportionate completion method

- Performance consists of execution of more than one act
- Revenue is recognised proportionately by performance of each act
- When indeterminate number of acts over a period of time, straight line recognition



Revenue from  
service transactions

## Completed service contract method

- Performance consists of execution of a single act  
Revenue is recognised only when services are completed or substantially completed
- If performance consists of more than one act and the act to be completed is **very** significant

**No significant uncertainty exists regarding the amount of consideration**

**It is not unreasonable to expect ultimate collection of consideration**



# Interest, Royalty and Dividend

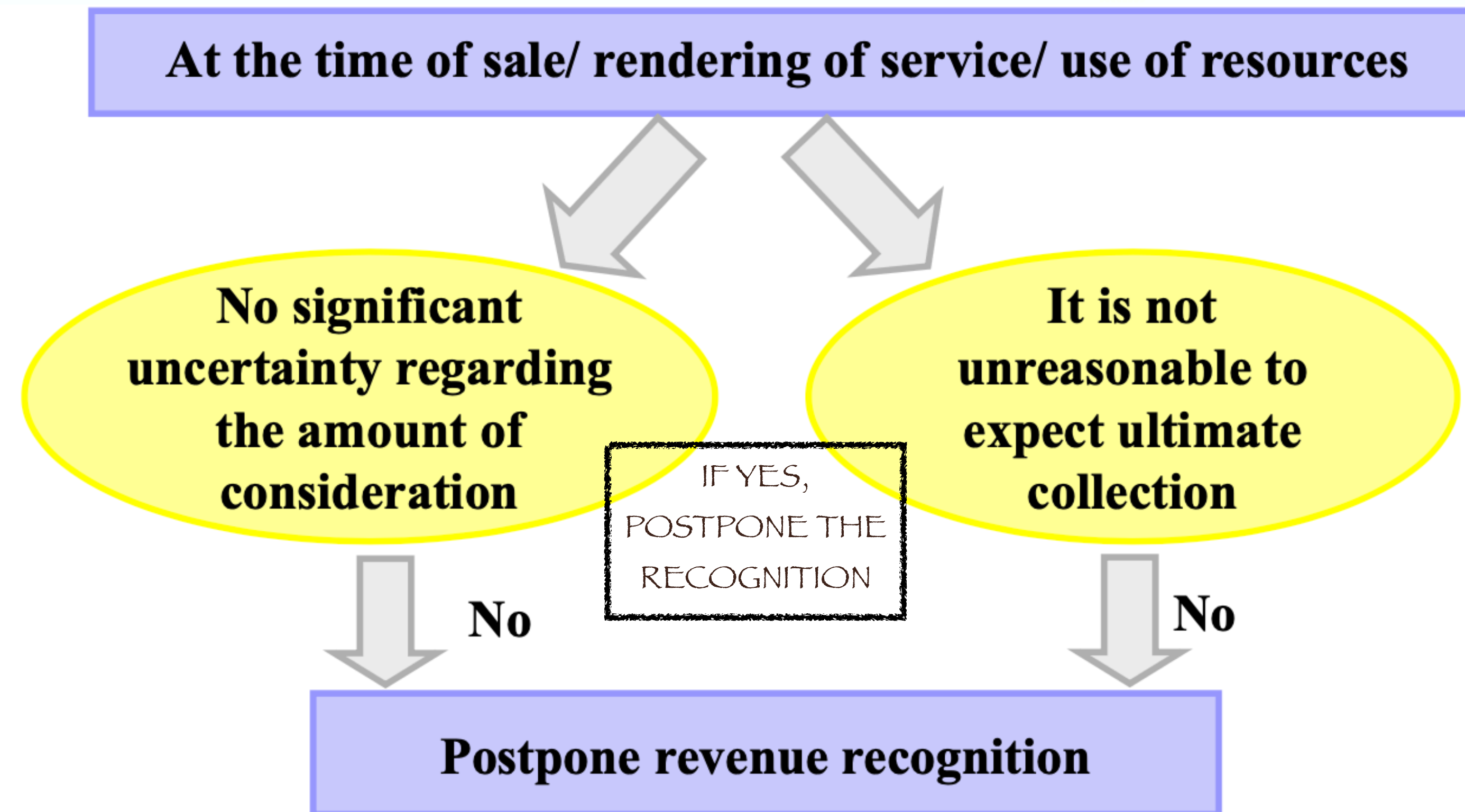
<b>Interest</b>	<b>Charge for use of cash resources or amounts due to the enterprise</b>	<b>Accrues on time proportion basis</b> <b>(taking into account the amount outstanding and the rate applicable)</b>
<b>Royalties</b>	<b>Charge for use of assets such as know how, patents, trade marks and copyrights</b>	<b>Accrual basis in accordance with the agreement (unless another basis is more systematic and rational)</b>
<b>Dividends</b>	<b>Rewards from the holding of investments in shares</b>	<b>When the right to receive dividend payment is established i.e. on declaration</b>

**No significant uncertainty exists regarding the amount of consideration**

**It is not unreasonable to expect ultimate collection of consideration**



# Effect of uncertainties on revenue recognition



- If uncertainty arises after recognising revenue, create a provision  
(do not adjust the revenue)
- Revenue realised, which was postponed due to uncertainties, is considered as revenue of the period in which it is properly recognised



## Special cases in case of sale of goods

### 1. **Delivery is delayed at buyer's request and buyer takes title and accepts billing**

Revenue should be recognised even if physical delivery has not been completed so long as there is every expectation that delivery will be made.

### 2. **Delivered subject to conditions**

(a) installation and inspection i.e. goods are **sold subject to installation, inspection** etc.

Revenue should normally not be recognised until the customer accepts delivery and installation and inspection are complete.

(b) **on approval**

Revenue should not be recognised until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed.

(c) **guaranteed sales i.e. delivery is made giving the buyer an unlimited right of return**

Recognition of revenue in such circumstances will depend on the substance of the agreement.

(d) **consignment sales** i.e. a delivery is made whereby the recipient undertakes to sell the goods on behalf of the consignor

Revenue should not be recognised until the goods are sold to a third party.

(e) **cash on delivery sales**

Revenue should not be recognised until cash is received by the seller or his agent.



**3. Sales where the purchaser makes a series of instalment payments to the seller, and the seller delivers the goods only when the final payment is received**

Revenue from such sales should not be recognised until goods are delivered. However, when experience indicates that most such sales have been consummated, revenue may be recognised when a significant deposit is received.

**4. Special order and shipments i.e. where payment (or partial payment) is received for goods not presently held in stock e.g. the stock is still to be manufactured or is to be delivered directly to the customer from a third party**

Revenue from such sales should not be recognised until goods are manufactured, identified and ready for delivery to the buyer by the third party.

**5. Subscriptions for publications**

Revenue received or billed should be deferred and recognised either on a straight line basis over time or, where the items delivered vary in value from period to period, revenue should be based on the sales value of the item delivered in relation to the total sales value of all items covered by the subscription.

**6. Instalment sales**

When the consideration is receivable in instalments, revenue attributable to the sales price exclusive of interest should be recognised at the date of sale. The interest element should be recognised as revenue, proportionately to the unpaid balance due to the seller.

**7. Trade discounts and volume rebates**

Trade discounts and volume rebates received are not encompassed within the definition of revenue, since they represent a reduction of cost. Trade discounts and volume rebates given should be deducted in determining revenue.



# Special cases in case of rendering of services

## 1. Installation Fees

In cases where installation fees are other than incidental to the sale of a product, they should be recognised as revenue only when the equipment is installed and accepted by the customer.

## 2. Advertising and insurance agency commissions

Revenue should be recognised when the service is completed. For advertising agencies, media commissions will normally be recognised when the related advertisement or commercial appears before the public. Insurance agency commissions should be recognised on the effective commencement or renewal dates of the related policies.

## 3. Financial service commissions

A financial service may be rendered as a single act or may be provided over a period of time. Similarly, charges for such services may be made as a single amount or in stages over the period of the service or the life of the transaction to which it relates. Such charges may be settled in full when made or added to a loan or other account and settled in stages..



#### **4. Admission fees**

Revenue from artistic performances, banquets and other special events should be recognised when the event takes place. When a subscription to a number of events is sold, the fee should be allocated to each event on a systematic and rational basis.

#### **5. Tuition fees**

Revenue should be recognised over the period of instruction/lectures.

#### **6. Entrance and membership fees**

Revenue recognition from these sources will depend on the nature of the services being provided. Entrance fee received is generally capitalised. If the membership fee permits only membership and all other services or products are paid for separately, or if there is a separate annual subscription, the fee should be recognised when received. If the membership fee entitles the member to services or publications to be provided during the year, it should be recognised on a systematic and rational basis having regard to the timing and nature of all services



# Disclosure

- Accounting policies for revenue recognition
- Circumstances in which revenue recognition has been postponed pending the resolution of significant uncertainties