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Revenue Recognition: Understanding the Impact of IFRS 15 - Revenue from Contracts with Customers

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Abstract

In May 2014, the International Accounting Standards Board issued International Financial Reporting Standard (hereafter IFRS) 15 “*Revenue from Contracts with Customers*”. The standard replaces the International Accounting Standards (IAS) 18, “*Revenue*” and IAS 11, “*Construction Contracts*.” The accounting guidelines under IFRS 15 will become authoritative in 2018. Some companies may not see significant changes in the amount of revenue recognized. However, in certain industries such as telecom, software development, real estate, and some retailers, the effect on revenue recognition timing may be significant. The purpose of this case is to contrast the accounting for a transaction under the present IAS standard for revenue recognition and the guidance to be implemented in 2018. The case is relevant not only for those majoring in accounting but also for majors such as finance that analyze corporate financial statements. The case requires the performance of a web search to obtain details of the guidelines provided in IFRS 15 and a contrasting of the accounting treatment under IAS 18 with the approach required by the new IFRS 15 for a mobile telecommunications company.

Key Words: Revenue Recognition , IFRS 15, “Revenue from Contracts with Customers”, International Financial Reporting Standard 15, telecommunications revenue recognition, telecoms revenue recognition, revenue recognition timing, five-step process for revenue recognition, guidance changes for revenue recognition, identify the contract with the customer, performance obligations, contract price, transaction price, satisfying the performance obligation.

Introduction

In May of 2014, the International Accounting Standards Board issued International Financial Reporting Standard (hereafter IFRS) 15 “*Revenue from Contracts with Customers*”. The standard replaces the International Accounting Standards (IAS) “*Revenue*” and “*Construction Contracts*” as well as several other interpretations dealing with related issues. The accounting guidelines under IFRS 15 were originally intended to become authoritative in 2017 however, following a recent amendment, this has been extended to 2018. IFRS 15 changes the guidelines for timing and amount of revenue recognition for contracts with customers. For many companies these changes will have little financial impact Companies in the telecoms, software development, real estate, and retail sectors may however be significantly impacted by these changes. The core of IFRS 15 is the new five step process for determining the timing and amount of revenue to be recognized which will now be applied to all revenue from contracts with customers.

What Are The Accountants Doing To Our Revenue?

The Company

MoServ is a Middle Eastern North African (MENA) telecommunications company that has been in existence since 2011. The company provides mobile phone service to 16 Middle Eastern and African countries. To attract customers they operate similar to their competition by offering low

cost or sometimes free mobile telephones to customers that sign multiyear service contracts. The company has been able to keep initial construction costs to a minimum by signing an agreement with a competitor to use the competitor's signal towers on a 10 year lease ending in 2022. MoServ has already begun to acquire land in suitable locations for construction of company owned signal towers. Financing of the tower construction will require the company to acquire external funding through debt issuances in 2021. The Treasurer is concerned about the potential impact of the adoption of IFRS 15 on the trading results for the company for the three years 2018 to 2020. The Treasurer has a finance background and needs to know the impact of the new revenue recognition guidelines on reported income in those two years. He requires guidance on the following issues:

- Will the effect lower reported earnings?
- If so, how much compared to earnings determined using IAS 18, the current guidance for revenue recognition?
- Will the amount of any decrease affect the cost of borrowing or perhaps even restrict access to some debt opportunities?

The treasurer has asked the Controller to assign an accounting staff member to report on the new IFRS 15 guidelines to bring the treasury staff up to date on the changes. He also wants to know how the new standard will affect the revenue recognition arrangements on their 2 year New Soltam contract. This is the company's highest revenue generating transaction and consists of a two year calling contract with a "free" telephone upon contract signing.

Revenue Transaction

MoServ offers a package similar to many of its competitors. Customers that sign up for a multiyear contract for phone usage are provided a phone for free or at cost significantly below the market value of the mobile phone. MoServ's main contract (that provides 95% of corporate revenue) is as follows:

2 Year New Soltam Contract with Moserv

Length of contract: 24 months

Cancellation policy: Non-cancelable

Monthly fee for mobile service: AED 800 (AED: United Arab Emirates currency)

Contract signing bonus: New Soltam 398FX6 sophisticated mobile phone

Other information:

Normal selling price of Soltam mobile phone without contract: AED 1800.

A 24 month contract with no free mobile phone is 870 AED per month.

The cost to MoSERV for the Soltam 398FX6 is AED 900 per unit.

Specific Instructions and Questions for the Accounting Staff

1. Access one of the websites of one of the Big Four public accounting firms and obtain the firm's publication on IFRS 15. You are looking for only an Overview of the guidance. The Treasurer only wants an introduction to the guidance not detailed information. Attach a file to your report with this information or publication for review by the Treasurer.

2. Is the new revenue recognition guidance different under IASB and FASB? Or is this a joint project where the guidance is similar?
3. Indicate the IASB standard that is followed currently by MoServ before the adoption of IFRS 15.
4. Show the accounting for the signing of one contract by a customer under the current IASB authoritative guidance, for revenue recognition. Include the accounting at the time of signing the contract and for the first two months of the contract.
5. What is the effective date for the adoption of IFRS 15?
6. Can MoServ adopt IFRS early?
7. List and discuss the five steps of revenue recognition under IFRS 15 as applied to MoServ's 2 Year New Soltam contract. Include the accounting journal entries at the time of signing the contract and for the first two months of the contract.
8. Write a brief description of the differences in the revenue and expense recognition under the two IASB standards.

The following step may or may not be assigned depending on the amount of time and depth desired by the instructor.

9. Complete a review of four articles written by the Big Four, accounting organizations or practicing accountants discussing the pros and cons of the new standard.

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