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FEATURES OF RECOGNIZING AND ACCOUNTING FOR REVENUE IN ACCORDANCE WITH IFRS 15

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Abstract. This article analyzes the provisions of IFRS 15 regarding the recognition and reporting of sales revenue in various situations. The article examines the provisions for reflecting revenue when providing discounts, gift certificates, warranties, etc. in accordance with the provisions of IFRS 15. A comparative analysis of the provisions for recognizing and measuring revenue in accordance with the provisions of IFRS 15 and NAS Revenue is also provided. It should be noted that Moldova signed the Agreement on Accession to the European Union, which requires bringing the country's regulatory and legislative acts into line with the requirements of the European Union. It should be emphasized that a number of provisions of NAS Revenue are already outdated and do not meet the requirements of IFRS 15. Therefore, the author proposes supplementing the balance sheet with a number of line items, introducing additional accounts into the chart of accounts, and modifying NAS Revenue in accordance with the provisions of IFRS 15.

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Introduction

International Financial Reporting Standard 15, "Revenue from Contracts with Customers," came into effect on January 1, 2018. This standard impacted revenue recognition and measurement for a number of companies in certain industries, such as telecommunications and construction companies, where contracts have multiple performance obligations. It should be noted that IFRS 15 replaced IAS 11, "Construction Contracts." However, there is no specific guidance for construction. Therefore, it was necessary to assess the adequacy of IFRS 15's guidance to address the complex challenges of the construction industry for recognizing revenue received under construction contracts. In their article, "The Adequacy of IFRS 15 for Revenue Recognition in the Construction Industry," M. V. Wyk and D. Coetsee examine the adequacy of applying this standard's provisions to construction contracts. In assessing the application of the principles of IFRS 15 to construction contracts, a structured approach was applied, based on the five-step model applied in IFRS 15. (V, 2020)

In his article Revenue Recognition: Five-Step Model, Jason Ochipa discusses the stages of sales revenue recognition, taking into account 5 stages. (Ochipa, 2023). The five-step model of IFRS 15 introduces a single model for accounting and determining when revenue is recognized, regardless of the type of transaction. This model must be applied to each individual performance obligation in a contract. The key principle of IFRS 15 is that an entity shall recognize revenue when it satisfies a performance obligation by transferring a promised good or service (i.e., an asset) to a customer. The asset is transferred when the customer obtains control of the asset.

At the same time, the standard specifies that an entity must apply this standard to all contracts with customers except contracts for:

- *leases,*
- *insurance,*
- *financial instruments and other contractual rights or obligations within the scope of IFRS 9 "Financial Instruments,"*

- *non-monetary exchanges between entities engaged in the same business to facilitate sales to potential customers.*

Analysis of IFRS 15 Provisions for Recognizing and Reporting Certain Revenue

One of the key changes introduced by IFRS 15 "Revenue from Contracts with Customers" is that revenue recognition is now based on the transfer of control of the goods or services to the customer (i.e., satisfaction of performance obligations), rather than simply the transfer of risks and rewards.

For many companies, this results in a change in revenue recognition pattern from gradual (over a period) to a one-time (point in time), or vice versa. In cases where the scheme for determining the moment of recognition remains unchanged, changes in the timing of the moment of recognition are possible.

Under IFRS 15, an entity must determine for each performance obligation whether control transfers:

- ✓ *over time, for example, as the obligations are satisfied, or*
- ✓ *at a point in time.*

If control does not transfer over time, the default is for the performance obligation to be satisfied at a point in time.

IFRS 15 sets out three criteria, at least one of which must be met for an entity to recognize revenue over time.

Table 1. Revenue recognition criteria in accordance with the provisions of IFRS 15

Criteria	Comments and guidance on the application of the standard	Examples
1.The buyer simultaneously receives and consumes the economic benefits provided by the company supplying the goods/services	o Typically applies to service contracts. o The concept of control of an asset applies because services are treated as an asset (at the same time) when they are received and used or consumed.	o Cleaning services, o Transportation services
2. The supplier creates or improves assets controlled by the customer	Typically applied when an asset (tangible or intangible) is created by the client.	A building constructed on land owned by the client. Software written on the client's existing IT infrastructure.
3. The supplier's fulfillment of its performance obligation; and - The supplier has the legal right to receive payment for the portion of the work completed to date under the contract.	o Typically used for construction/development of assets to customer specifications	Construction and real estate (developers) Manufacturing and engineering contracts for specialized products/assets Certain advertising and consulting services

Source: developed by the author in accordance with the provisions of IFRS 15

When recognizing revenue at a point in time, entities must consider when the customer obtains direct use of the received asset and obtains substantially all of the remaining benefits from the asset. IFRS 15 includes a list of indicators that the customer has obtained control of the asset, including:

- *The customer has a present obligation to pay,*
- *The customer has physical possession of the asset,*
- *The customer has legal title,*
- *The customer has accepted the risks and rewards of ownership,*
- *The customer has accepted the asset.*

For example, some consumer goods manufacturers and retailers supply goods on a "free on board" (FOB) basis. That is, control of the asset is transferred when the asset is loaded on board the vessel. However, suppliers bear a certain degree of risk during loading and may conclude that control transfers (based on legal title, the right to payment, or the customer's right to redirect the goods) before the risks and rewards are transferred and may recognize revenue earlier in accordance with IFRS 15.

According to the National Accounting Standard "Revenue," revenue in the Republic of Moldova includes receipts of economic benefits received or receivable by entities in their own name. Revenue is measured at the fair value of the consideration (means of payment) received or receivable, less any price reductions, bonuses, and other trade discounts granted by the seller. Fair value is the estimated selling price of a single asset in an orderly transaction between interested, independent, and knowledgeable parties.(NAS Revenue)

Retail chains often offer customers gift cards that can be used to pay for purchases at a later date. For example, a customer might purchase a gift card for $100 and give it to someone as a birthday present. The cardholder can then return to the store and purchase something using the gift card.

Gift cards are unexercised rights of customers that will be exercised in the future. The amount related to this unexercised right must be recognized as a contractual liability. When a customer arrives at a store, purchases a product, and pays with a gift card, that's when revenue from the sale must be recognized.

This is also known as the breakage amount—prepaid but unused service. The unexercised portion must be recognized as revenue proportionate to the structure of the rights the customer exercises.

In the case of a gift card, this depends on how the customer can use it:

- *If the customer can only use it for a single payment, the entity recognizes the unused portion of the card as revenue when the customer uses it.*
- *If the customer can use the card until they spend the entire amount, the entity recognizes revenue proportionately.*

If a gift card is not used for a long time and does not expire, then it is necessary to collect some statistics for past periods to estimate how much time must pass before the customer forgets about unused gift cards and the likelihood of them using them becomes insignificant and then reflects this on revenue.

If a gift card is provided as a bonus, meaning the card is provided upon a purchase under certain conditions, then the transaction price must be split and allocated between the goods sold and the gift cards in proportion to their relative stand-alone selling prices. Example of accounting for gift cards provided as a bonus.

Conditional example 1: The entity offers a free $10 gift card if a customer makes a purchase of more than $100. The customer purchases a product for $100 and receives a $10 gift card. The total transaction price is $100 because this is the amount the entity will receive from the customer for the product and the gift card. Therefore, the transaction price of $100 must be allocated among the individual performance obligations based on their relative stand-alone selling prices.

Table 2. The price allocation calculation is presented between individual performance obligations based on relative stand-alone selling prices

Performance Obligation	Standalone selling price	Distribution of transaction price
Goods	100	91 (100/110*100)
Gift Card	10	9 (10/110*100)
Total	**110**	**100**

Source: developed by author

Accordingly, the accounting entries for the issuance and sale of a gift card will be as follows:

Debit Cash - $100
Credit Revenue from Sales of Goods - $91
Credit Contract Liability (Gift Cards) - $9

If a customer purchases goods for $10 and pays with a gift card, this transaction is reflected by the following accounting entry:

Debit Contract Liability (Gift Cards) - $9
Credit Revenue from Sales of Goods - $9

If the customer does not redeem the gift card and it expires, the accounting entry will be the same, but revenue will be recognized as "revenue from the unclaimed portion of the gift card."

IFRS 15 "Revenue from Contracts with Customers" addresses the accounting for customer loyalty programs using discount coupons and points [4]. However, the standard also contains a significant number of more detailed additional requirements for applying the five-step model. Two areas are particularly important for accounting for marketing promotions:

o Unexercised customer rights (loss of coupon);

o Optional provision of additional goods or services to the customer (customer loyalty programs).

In both cases, applying IFRS 15 will defer revenue recognition until additional goods or services are transferred to the customer in exchange for discount coupons.

When a customer purchases a gift voucher that can be redeemed for goods or services, the retailer recognizes a contract liability. For example, a retailer sells a gift card for $100. Based on historical data, the retailer believes that $10 of the gift card will ultimately not be redeemed, but can demonstrate this expectation with a high probability only for $6 of the gift card. In this case, the retailer should recognize revenue of $1,064 for each $1 redeemed.

IFRS 15 also addresses revenue recognition when optionally providing additional goods or services to a customer (loyalty programs). For example, when a customer purchases goods from a seller, they receive points or discount coupons that can be used to obtain additional goods or services from that seller or to receive a discount on future purchases of goods or services. IFRS 15 requires that such offers be treated as a separate obligation if they constitute a "material right" of the customer. (IFRS 15) A material right is a right that the customer would not have had without the initial purchase. For example, a discount coupon containing a clause such as "10% off your next purchase" granted as a result of a sale would only constitute a material right if the seller did not offer such a right free of charge in advertisements.

Another important point concerns the distinction between contract assets and receivables. IFRS 15, "Revenue from Contracts with Customers," introduced the concept of a contract asset. A contract asset, as defined in the appendix to IFRS 15, is an entity's right to consideration in exchange for goods or services it has transferred to a customer when that right is contingent on something other than the passage of a specified period of time, such as the entity's future performance of specified obligations.

A trade receivable (or account receivable) is a financial asset under IAS 32 Financial Instruments: Presentation and is defined as a contractual right to receive cash or another financial asset from another entity. (IAS 32)

The primary difference between a contract asset and a trade receivable is conditionality. A contract asset is a conditional right, while a trade receivable is an unconditional right. A contract asset arises when a supplier has already performed something as agreed (delivered some goods or services), but under the terms of the contract still has to deliver something before it can invoice the customer for payment. Let's consider an example to understand how this asset differs from accounts receivable from customers.

Conditional example 2: A client has commissioned the construction of a building. The project will take nine months and begins on July 1. The total contract price is $100,000. In the contract, the developer agreed that the client will pay for the entire project when the building is completed and the property is handed over to the client. At the end of the year, after six months of work on the project, in accordance with IFRS 15, the developer must recognize revenue based on the assessed progress of fulfilling the performance obligation. Let's assume the project is 70% complete, so revenue equal to 70% of the total transaction price, or $70,000, should be recognized.

The accounting entry for recognizing the contract asset is as follows:

Debit Contract Asset - $70,000

Credit Sales Revenue - $70,000

The reason the receivable won't be recognized is that at the end of the year, after six months of work, the developer doesn't have an unconditional right to receive payment. Before receiving cash, the construction company must fulfill the contractual condition—complete the project. Then, the construction company works for another three months, completes the project, and hands it over to the client. At that point, it has an unconditional right to payment, not a contract asset.

The construction company's accounting entries after project delivery will be as follows:

Debit Account Receivable - creation of an unconditional right to receive payment upon project delivery to the client - $100,000

Credit Contract Asset - a conditional right recognized at the end of the previous year that has become an account receivable or an unconditional right - $70,000

Credit Revenue - revenue recognition for the last 3 months based on the assessment of the degree of fulfillment of the performance obligation - $30,000

Another key issue addressed by IFRS 15 "Revenue from Contracts with Customers" is the accounting for product warranties. Let's examine the provisions of IFRS 15 using a hypothetical example.

Conditional example 3: A company sells 100 units of a product at a price of 10. The unit cost is 8, and the gross profit, accordingly, is 2. The company expects 12 units to be returned for a refund or exchange.

Table 3. Comparison of sales revenue recognition under IAS 18 and IFRS 15

Indicators	According to IAS		According to IFRS 15	
	Amount	Calculation	Amount	Calculation
Revenue	1 000	(100 * 10 y.e.)	880	(100-12) * 10 y.e.
Cost of sales	824	100* 8 y.e. + 12* 2 y.e.	704	(100-12) * 8 y.e.
Gross profit	**176**		**176**	
Stocks	-		96	12 * 8 y.e.
Refund obligation	24	12 * 2 y.e.	120	12 * 10 y.e.

Source: developed by author

Although gross profit remains unchanged, revenue, which is likely a key performance indicator for management, may decline significantly. Therefore, it becomes clear that after the transition to IFRS 15, assessing the expected volume of returns is critical, especially for retail companies.

IFRS 15 provides some clarification on the provision of product warranties. Assume that a company provides a one-year warranty on all its products in accordance with local law, but a customer can extend this warranty for three years for a fee. When determining the recognition and accounting for warranties, paragraphs B28-B33 of IFRS 15 should be applied, which note that there are two main types of warranties:

• *Assurance*-*type warranties are warranties that assure the customer that the delivered product meets the contractual requirements and will perform as specified in the contract. These warranties do not give rise to a separate performance obligation, and only a provision for warranty repairs is accounted for in accordance with IAS 37 "Provisions, Contingent Liabilities, and Contingent Assets."*

• *Service*-*type warranties are warranties that provide something in addition to a simple warranty, such as providing some additional service. These warranties give rise to a separate performance obligation because they provide an additional service to the customer and are accounted for in accordance with IFRS 15.*

Therefore, the first step is to classify these warranties and determine whether the customer has the option to purchase a separate warranty. If so, it is an extended warranty and should be considered a separate performance obligation. If not, it is necessary to determine whether the warranty provides the right to more than just the warranty for defects existing at the time of sale. It is also important to consider whether this warranty is required by law. Many countries have laws requiring a warranty for a certain minimum period. If the warranty is of this type, it is a standard warranty and does not constitute a separate performance obligation. Is the warranty provided for a longer period than required by law? If so, it is an extended warranty.

Conditional example 4: A company sells refrigerators for $100, and the official warranty period is 2 years. During these 2 years, the company must correct all defects that existed at the time of sale. Customers can extend this warranty for an additional 2 years for a fee of $20. The company estimates the discounted cost of repairs at $40,000 for the first 2 years (years 1 and 2 after purchase) and $50,000 for the next 2 years (years 3 and 4 after purchase).

In this case, the first 2 years of the warranty period are considered a standard warranty, since this warranty cannot be purchased separately—it is provided for by law. Accordingly, a provision must be made, as required by the provisions of IAS 37 (IAS 37).To create a reserve for warranty repairs in the amount of the estimated cost of repairs over the next two years, the following accounting entry will be made:

Debit Warranty Repair Expenses account - $40,000

Credit Warranty Repair Reserve account - $40,000

When warranty repairs occur during the first two years, the company writes off the actual expenses to reduce the reserve.

In the case of an extended warranty, which represents a separate performance obligation because the customer effectively pays for it separately, the extended warranty represents a separate performance obligation. When a customer purchases a refrigerator for $100 with an extended warranty, the total purchase price is $120. The company accounts for this extended warranty as a separate performance obligation and recognizes revenue when the performance obligation is satisfied. Revenue from the sale of the refrigerator is recognized immediately upon sale because that is when the refrigerator is delivered to the customer and the performance obligation is satisfied.

A very important point to note is the recognition of revenue from the provision of services and the performance of work. IFRS 15 provides two methods for measuring the progress of work if revenue under a contract with a customer is recognized over time. Let's consider the specifics of revenue determination using the output method and the input method:

o *The output method, which is based on an assessment of the degree of readiness of the asset transferred to the client, or*

o *The input method, which is based on an assessment of the degree of consumption of resources used to create the asset transferred to the client.*

The output method uses a direct measurement of the value of goods or services transferred to the customer as of the current date. This includes valuing the results achieved, completed work stages, and units produced or delivered. For example, after two floors of a ten-story building have been constructed, 2/10ths of the total contract revenue is recognized.

The input method is based on the effort or materials expended by the company to fulfill the performance obligation. This means revenue is estimated based on the resources consumed, labor time expended, costs, machine time expended, etc. For example, if $100,000 has been expended and the total estimated project cost is $1 million, 1/10th of the project revenue is recognized.

Conclusions

Revenue is not only an economic indicator of a company's performance but also the basis for forecasting its activities. The correct accounting of revenues determines the correct formation of a company's financial results and the ability to effectively budget for long-term revenues, including by type of activity.

In light of Moldova's accession to the European Union, there is an urgent need to revise accounting regulations and bring them into line with EU requirements. This primarily applies to the provisions of accounting standards and specifically to the National Standard "Revenue." It should be noted that NAS "Revenue" was written and applied prior to the entry into force of IFRS 15, so many provisions for revenue recognition and measurement in accordance with national requirements are now outdated and require revision. In this regard, the Republic of Moldova needs to:

1) Revise its accounting regulations to ensure compliance with EU regulations, namely the Law on Accounting and Financial Reporting and National accounting standards, including the National Accounting Standards (NAS) "Revenue";

2) Introduce new definitions in the NAS "Revenue" (for example, contract asset);

3) Modify the chart of accounts by introducing new accounts, such as a contract asset account;

4) Revise the financial statements, including the balance sheet, by modifying and adding new line items to the balance sheet asset.

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