

SPECIAL GAAP REPORT

‘AASB 15’

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AASB 15 – the effective date approaches

Don't stick your head in the sand

JANUARY 2018, the new effective date of AASB 15, might seem a long way off. It isn't, particularly when you start examining the new standard's detail.

Entitled *Revenue from Contracts with Customers*, AASB15 supersedes AASB 118, *Revenue*, and AASB 111, *Construction Contracts*, as well as some accounting interpretations.

AASB 15 (and its international equivalent IFRS 15) are effective for annual reporting periods commencing on or after 1 January 2018. Most Australian entities will be adopting this standard in their 30 June 2019 reporting periods.

Why should entities think about AASB 15 now?

Let's start with the most technical reason. Paragraph 30 of AASB 108, *Accounting Policies, Changes in Accounting Estimates and Errors*, requires entities to disclose the effect of standards issued that are not yet effective in all financial statements from the date of issue to the date of adoption. As we move towards AASB 15 effective date, an entity should be able to quantify its affect.

Now a few more practical, operational reasons.

AASB 15 is likely to result in changes to your IT systems, reported results, customer contracts, bonus schemes, bank covenants, budgets, accounting manuals and disclosure templates.

Implementation of AASB 15 will be the responsibility of not only your finance team. Various staff will need to be involved to ensure that the transition is accurate, seamless and minimises stakeholders' surprises.

The time needed to determine the impact of AASB 15 on an entity will be significant. Each aspect of the contract and revenue process will need to be scrutinised, and a plan for implementation developed.

Below is a time-frame for implementation.

	December reporting period	June reporting period
AASB 15 effective date	31/12/2018	30/6/2019
Comparative balance sheet date	31/12/2017	30/6/2018
Opening balance sheet date/ transition date	1/1/2017	1/7/2017

AASB 15 does permit an entity to adopt a modified retrospective approach to transition, which requires changes to be made at the beginning of the comparative period or a full retrospective approach. Regardless of the approach adopted – there is not a lot of time to complete potential system changes, contract alterations, stakeholder communications and so on to be able to prepare an opening balance sheet.

You may adopt the standard early, but we expect that few entities will use this option.

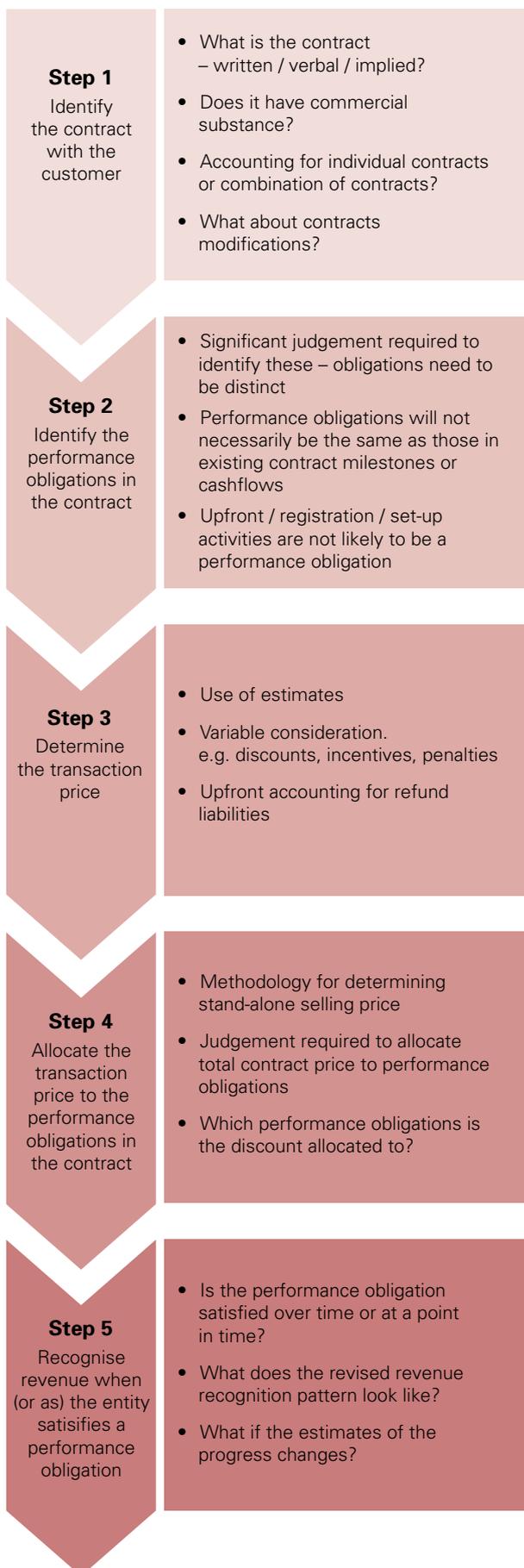
AASB's key principles

'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.'

What does this actually mean?

AASB 15 has introduced five steps that need to be satisfied before an entity can recognise revenue. They're summarised in the diagram on the following page.

Five steps that need to be satisfied before an entity can recognise revenue



Legal considerations with Stephen Newman, Hope Earle

Step 1 requires the identification of a contract that creates **enforceable rights and obligations**. This raises a number of possible legal questions including:

- Does a contract exist – do we have the elements of intention to create legal relations, offer and acceptance and consideration for the contract?
- Has the contract been properly signed such that it can bind the signing party?
- If a written contract exists, are all the terms in it such that what the parties have agreed is certain?
- Does the written contract reflect the bargain the parties intended to strike and if not, can the contract be rectified as a matter of law?
- If the terms of the contract are certain, is the contract vulnerable to attack because there has been a breach, for instance, of the Australian Consumer Law or because it offends some other legislation or legal principle?
- If the written contract is ambiguous or uncertain, are there terms that can be implied as a matter of law that might overcome these problems?
- If the contract is verbal or partly verbal and partly in writing, how do I determine what the contract is?
- If there is no contract, can one or more parties still assert that they have legal rights to compel the transfer of goods or services (in other words, does the law of estoppel apply)?
- If the contract is not governed by a 'legal framework', is it governed by an 'equivalent framework' (for instance, Sharia Law) such that it can be said that enforceable rights and obligations and performance obligations exist?

These are not academic legal questions; they constantly arise in practice. AASB 15 will require accountants and auditors to take a more considered approach to the 'contract question' than they might have previously done.

Other areas to consider

As with many things, the devil is in the detail of AASB 15 so don't forget to think about issues such as:

- Contract costs** – The costs to obtain and fulfil a contract are capitalised if certain conditions are met. This has been the practice with construction contracts within the scope of AASB 111 in the past, but it is now relevant for all contracts with customers. The amortisation period needs to be determined.
- Transitional guidance** – AASB 15 provides a choice on transition of either:
 - Full retrospective approach – that is, restating revenue relating to contracts in place at the transition date in accordance with AASB 15.
 - Partial restatement approach – apply AASB 15 for the current year only, that is, restating contracts in place at the beginning of the current reporting period and recognising changes in the current year. Additional disclosures need to be provided if this approach is used.
- Contract modifications** – If the contract is modified by any party, then an assessment is required regarding whether the modification is, in effect, a separate contract or whether it is a modification of the existing contract, which would result in a revision of assumptions made to date.
- Rights of return** – Estimates of the expected refund liability and associated asset is to be determined at inception date and revised at each reporting date. Changes in value are adjusted against revenue rather than in an expense account.

e. **Disclosures** – Existing standards have minimal disclosures in relation to revenue. This is not the case under AASB 15. Disclosures are extensive and will need to be carefully considered with respect to information provided to the market. Additional disclosures include:

- Information about contract balances
- Information about performance obligations
- Explanations of significant judgements
- Assets recognised in relation to the obtaining or fulfilment of contracts.

Industry focus – construction contracts

Since AASB 15 replaces the current construction contracts accounting standard, AASB 111 Construction Contracts, entities operating in the construction industry or who use AASB 111 as an analogy for their existing long-term projects will find that the percentage of completion method as we currently know it will no longer exist. Current contracts and revenue recognition policies will have to be reviewed as existing milestones in contracts will not necessarily meet the definition of performance obligations and the gap between date of cash receipts and revenue recognition may grow wider.

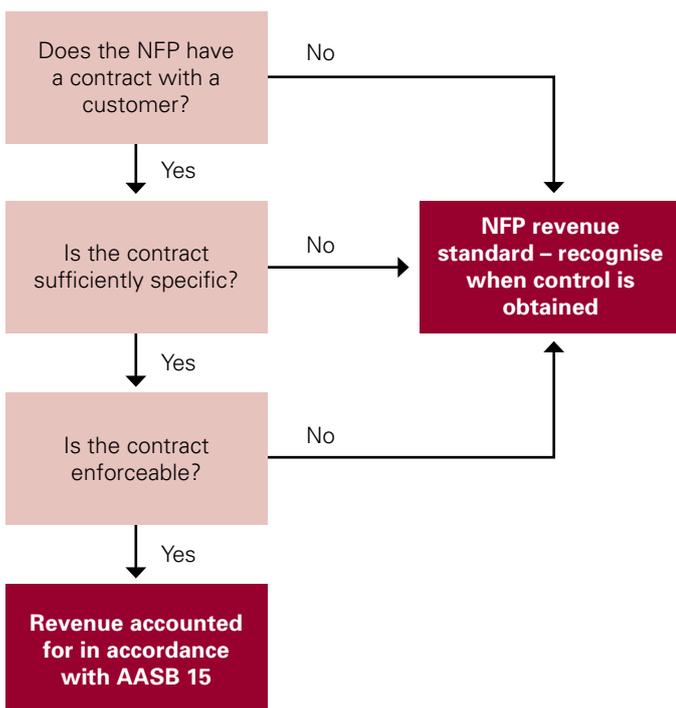
Implications for Not-For-Profit (NFP) entities

The AASB are considering feedback received on the exposure draft 'Income of Not-for-Profit Entities' that was issued in 2015.

We expect to see a final standard in 3rd quarter 2016 which will direct NFPs to follow the requirements of AASB 15 where they have a contract with a customer which is sufficiently specific and enforceable. An appendix to AASB 15 will assist NFPs in applying the standard.

A specific NFP revenue standard will also be issued for contracts that are not in the scope of AASB 15. This will require revenue recognition once control of the funds is obtained (likely to be on receipt).

This can be summarised in the diagram below.



To do list

- Find time to consider AASB 15 – we are all busy but this can't be ignored
- Understand existing revenue-recognition practices, including reviewing existing contracts with customers
- Read AASB 15 in the context of your organisation and existing contracts – identify areas of potential change
- Apply the requirements of AASB 15 to your existing contracts and understand their impact
- Form an implementation committee with representatives from relevant divisions or external advisors (legal, finance, sales, contract management, project management)
- Identify deficiencies in existing systems that will prevent your capturing relevant AASB 15 information
- Determine whether changes to existing contracts are needed
- Formulate a communications strategy for key stakeholders, for instance, banks, shareholders and most importantly customers
- Develop a project plan and
- Seek expert assistance.

GAAP Consulting's experience to date

Impact analysis of AASB 15 have now been performed by GAAP Consulting for several entities. Some key outcomes from these projects:

- Upfront administration and set-up costs cannot be recognised immediately – this revenue and associated costs are spread over the terms of a contract. Revenue might go through operating profit twice
- Where there is a period of more than 12 months between receipt of cash and transfer of control over goods/services then need to consider whether there is a significant financing component and whether discounting needs to be applied
- Time needs to be spent developing a process to identify contract costs to be capitalised
- Amendments to contracts to more clearly articulate performance obligations or to include terms about entitlement to payment for work performed to date
- Treatment of loyalty schemes, gift cards, vouchers etc
- Calculations of variable consideration and developing processes for this to be performed on a consistent basis across contracts
- Judgement around identification of refund liabilities and quantifying these.

Today's take-away

AASB 15 is more prescriptive than previous standards	Effective for 31 December 2018 / 30 June 2019 year ends	Retrospective application means opening balance sheets at 1 January 2017 or 1 July 2017
What is the methodology for estimating variable consideration, e.g. discounts, claims, incentives?	The actual impact of AASB 15 will vary per entity but all entities will need to go through the process to assess impact	Which costs are going to be capitalised? Are the systems in place to capture these?
AASB 15 is not just an issue for finance teams.	Performance obligations are not necessarily your existing contract milestones	ASIC has included AASB 15 standards issued not yet effective disclosure as a focus – don't use boilerplate

The breadth and depth of the technical services we provide is considerable. Our team members are authoritative, knowledgeable and have a profound understanding of accounting standards and the regulatory environment. *GAAP Consulting* has eight multi-skilled, recognised experts, all of whom are partner equivalents.

Talk to the GAAP Consulting team to help you understand and implement AASB 15 *Revenue from Contracts with Customers*. GAAP consulting provides with access to some of Australia's best.



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Carmen Ridley is an expert in financial reporting who was previously Associate Director in the technical team at Grant Thornton, National Technical Director of William Buck, and author of 'Understanding and Implementing the Reduced Disclosure Regime',

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Stephen Newman is a corporate and commercial lawyer who also has considerable litigation and dispute-resolution experience.

He has been a partner in well-known Melbourne CBD law firms and is now with Hope Earle Lawyers. He works closely with the GAAP Consulting team in providing advice on a range of matters, including the

application of the Corporations Act 2001 to audit practice, the ASX Listing Rules, the application and interpretation of the auditing and accounting standards, audit-practice risk management, fraud detection and investigation, preparation of section 311 reports to ASIC, dealing with ASIC investigations and enforcement proceedings and auditor negligence and other civil claims.

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