International accounting standards: revenue recognition

Introduction This assignment features the recognition and measurement of revenue depending on the source of revenue in accordance with the provisions of International Accounting Standards (IAS) 18 Revenue. I researched the topic and defined the special purposes of the assignment: first of all, it is important to know the main concepts of IAS 18, also to learn the rules by using this particular regulatory framework, and to get knowledge about writing the report at all. The Report To: Managing Director

From: Student A Regarding: IAS 18 Date: 3/11/2011 Introduction to the Report The Conference on International Accounting Standard (IAS) 18 Revenue was held to introduce the concepts of the regulatory framework of financial reporting and to represent the given information in convenient use of practice. The objective of IAS 18 is to prescribe the accounting treatment for revenue arising from certain types of transaction and events (Summaries of International Financial Reporting Standards, 2001). Key definition

According to International Accounting Standard Committee (IASC) the Framework Revenue is income that arises in the course of ordinary activities of an enterprise and is referred to by a variety of different names including sales, fees, interest, dividends and royalties (IASC, 2000). So revenue is one of the most important indicators of accounting. It is a key factor of the profit, its assessment helps to build many financial indicators on the profitability of the activities of the organization, as well as return on investment.

A key issue when recording revenue is to define the moment of its recognition. Revenue is recognized if it is likely that the organization will receive economic benefits in the future, and these benefits can be reliably measured. IAS 18 specifies conditions where these criteria are met and therefore the revenue recognizes. This standard also provides practical advice on the application of those criteria. Measurement of Revenue In accordance with IAS 18 revenue is usually determined by agreement between the supplier and the customer or user of the asset.

This means that it is measured at fair value consideration, which the company has received or receivable; trade discounts and volume rebates provided by the enterprise are taken into the amount. The standard defines fair value as " the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction". (IASC, 2000) As the fair value is often expressed in monetary terms, the revenue will be the amount that the company has received or receivable. This problem occurs when the incoming payment is deferred.

In this case the present value of the payment will be less than its face value. So IAS 18 introduced the following requirement: the company must be discounting. In such circumstances all future receipts should be discounted using the imputed interest rate. The second problem in recognizing the revenue arises in cases when the company offers its clients discounts for fast calculation. To comply with the requirements of IAS 18, discounts for fast payment should be measured at the time of the sale and deduct from the revenue.

In cases when there is an exchange for goods or services similar in nature, cost of revenue does not arise. When exchanging a variety of goods, revenue is measured at fair value of the goods or services received, minus the amount transferred to cash or cash equivalents. Revenue recognition Revenue is recognized with regard to the certain points: the convincing evidence of an agreement with a customer, the delivering goods and the rendering of services. Sale of goods

There are following criteria to recognize revenue from the sale of goods: * Significant risks and rewards associated with ownership of the goods passed from the seller to the buyer; * The company no longer participates in the management of the property, sold goods and it does not have control over them; * The amount of revenue can be reliably assessed; * Costs that should be suffered relating to a transaction can be measured reliably; * There will be probable economic benefits for the enterprise as a result of this operation. Rendering of services

When the outcome of a transaction involving the rendering of services can be reliably estimated, revenue from the sale of services is based on the level of completion of the transaction at the balance sheet date. The outcome of a transaction can be measured reliably when: * The amount of the transaction can be reliably assessed; * There will be probability to get economic benefits for the enterprise as a result of this operation; * Level of completion of the transaction at the balance sheet date can be assessed; * Costs that should be suffered relating to a transaction can be measured reliably.

Revenue from the provision of goods and all services is only recognized when the amounts to be recognized are fixed or determinable, and collectability is reasonably assured (Elliot B. , Elliot J. , 2007) Interest, royalties and dividends IAS 18 considers the accounting procedure of potential components of revenue organization primarily from transactions involving the sale of goods, rendering of services, as well as through other organizations or individuals property of the reporting organization, giving interest, dividends or royalties.

If the probability of the economic benefits for the enterprise exists and the amount of revenue can be measured reliably, income in the form of interest, royalties and dividends are recorded as follows: * Interest (fees that are levied for the use of cash and cash equivalents or amounts owed) should be recognized on a temporary basis, which is proportional to the effective yield of the asset; * Dividends (profit-sharing between the owners of the share capital in proportion to their participation in the capital of a particular class) should be recognized when the shareholders have the right to receive payment; * Royalties (fees for the use of fixed assets such as patents, trademarks, copyrights and computer software payments) should be recognized on an accrual basis according to the content of the relevant treaty. Disclosure requirements IAS 18 contains certain disclosure requirements because it is important to use disclosures to get the decision-useful information about an entity’s arrangements with customers.

In the income statement, as well as in the financial statements should be disclosed the following information: a. The amount of each substantive article of the revenue received from the sale of goods, services, as well as the amount of interest, royalties and dividends; b. The amount of revenue arose from exchanges of goods or services; c. The methods used to designate the quantitative measures for the level of completion of the transactions in rendering of services. The disclosure requirements provide sufficient information to users of an entity’s financial statements about the changes in circumstances affecting those performance obligations

(International Accounting Standards Board, 2008). Example of Revenue On 1/04/2010 Leather Ltd. eceived total subscriptions of €480, 000. So as the result, the company is obliged to provide 24 monthly publications of the magazine. Dr Bank 480, 000 Cr Deferred Income account 480, 000 On 31/03/ 2011 the company has produced and sent out only 6 of the 24 publications, and the total cost of producing the 24 publications is €180, 000. The average cost of each publication is the same amount. That means each publication cost 7, 500 (€180, 000/24). Consequently, the cost of production 6 publications is €45, 000 (€7, 500*6). For one year, from 1/04/2010 to 31/3/2011, company produced 6 publications. Therefore, to produce all 24 publications, the company should complete the order in 4 years.

Thus, each year Leather Ltd. will earn €120, 000 (€480, 000/4) selling 6 publications. The organization will receive economic benefits in the future, and these benefits can be measured reliably. So 31/3/2011 revenue of the company is €120, 000. Dr Deferred Income account 120, 000 Cr Sales account 120, 000 Income Statement of Leather Ltd. for the year ended 31st March 2011 Sales 120, 000 Cost of production 45, 000 Gross profit 75, 000 Conclusion of the Report Revenue recognition criteria provided in IAS 18 " Revenue" should normally be applied to each operation separately.

However, in certain circumstances, they must be applied to individual elements of a transaction in order to correctly reflect the sources of revenue. At the same time, on the contrary, recognition criteria can be applied simultaneously to two or more operations when their commercial effect cannot be determined without considering the operations as a whole. The provided conference helps to understand that the general principles of revenue recognition and measurement for financial reporting are extremely essential in the system of accounting rules formed by IAS. Signed: ____________ Conclusion The assignment represents the report that determines the important concepts of the regulatory framework defined by IAS 18 Revenue.

While researching the following topic I got useful knowledge about the structure of the report. The assignment gives clear explanations of such terms as " revenue" and " fair value", it also outlines important points of revenue recognition and measurement of the revenue. The assignment covers all information about how to recognize revenue and there is the particular example on revenue recognition. Bibliography ELLIOT, B. , ELLIOT, J. , (2007). Financial Accounting and Reporting. Accounting and reporting on an accrual accounting basis. 11th edition. London: Copyright Licensing Agency Ltd. , p. 26. International Accounting Standards Committee (2000). International Accounting Standards Explained.

Accounting for revenue and Expenses Revenue. London: Copyright of IASC, p. 321. International Accounting Standards Committee (2000), International Accounting Standards Explained, Accounting for Revenue and Expenses Revenue. London: Copyright of IASC, p 322. Preliminary Views on Revenue Recognition in Contracts with Customer. International Accounting Standards Board, 2008. p. 77 http://www. iasb. org/NR/rdonlyres/0E3D5E00-B961-42F0-BA64-AB1D20BB9FE9/0/DP_PreliminaryViewsRevenueRecognition1208. pdf Accessed: 24 Oct 2011 Summaries of International Financial Reporting Standards. Deloitte, 2001. http://www. iasplus. com/standard/ias18. htm. Accessed: 20 Oct 2011