Introduction

This Standard deals with the bases for recognition of revenue in the statement of profit and loss of an enterprise.

It is concerned with the recognition of revenue arising in the course of the ordinary activities of the enterprise from

- the sale of goods,
- the rendering of services, and
- the use by others of enterprise resources yielding interest, royalties and dividends.
It does not deal with the following aspects of revenue recognition to which special considerations apply:

- Revenue arising from construction contracts
- Revenue arising from hire-purchase, lease agreements
- Revenue arising from government grants and other similar subsidies
- Revenue of insurance companies arising from insurance contracts.
Introduction (Contd.)

Examples of items **not included within the definition of “revenue”** for the purpose of this Standard are:

- Realised gains resulting from the disposal of, and unrealised gains resulting from the holding of, non-current assets e.g. appreciation in the value of fixed assets;
- Unrealised holding gains resulting from the change in value of current assets, and the natural increases in herds and agricultural and forest products;
Realised or unrealised gains resulting from changes in foreign exchange rates and adjustments arising on the translation of foreign currency financial statements;

Realised gains resulting from the discharge of an obligation at less than its carrying amount;

Unrealised gains resulting from the restatement of the carrying amount of an obligation.
**Definitions**

**Revenue** is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise from the sale of goods, from the rendering of services, and from the use by others of enterprise resources yielding interest, royalties and dividends. It is measured by the charges made to customers or clients for goods supplied and services rendered to them and by the charges and rewards arising from the use of resources by them. In an agency relationship, the revenue is the amount of commission and not the gross inflow of cash, receivables or other consideration.
Definitions

**Completed service contract method** is a method of accounting which recognises revenue in the statement of profit and loss only when the rendering of services under a contract is completed or substantially completed.

**Proportionate completion method** is a method of accounting which recognises revenue in the statement of profit and loss proportionately with the degree of completion of services under a contract.
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.
Sale of Goods

A key criterion for determining when to recognise revenue from a transaction involving the sale of goods is that the seller has transferred the property in the goods to the buyer for a consideration.

The transfer of property in goods, in most cases, results in or coincides with the transfer of significant risks and rewards of ownership to the buyer. However, there may be situations where transfer of property in goods does not coincide with the transfer of significant risks and rewards of ownership.
Revenue in such situations is recognised at the time of transfer of significant risks and rewards of ownership to the buyer. Such cases may arise where delivery has been delayed through the fault of either the buyer or the seller and the goods are at the risk of the party at fault as regards any loss which might not have occurred but for such fault. Further, sometimes the parties may agree that the risk will pass at a time different from the time when ownership passes.
At certain stages in specific industries, such as when agricultural crops have been harvested or mineral ores have been extracted, performance may be substantially complete prior to the execution of the transaction generating revenue.

In such cases when sale is assured under a forward contract or a government guarantee or where market exists and there is a negligible risk of failure to sell, the goods involved are often valued at net realisable value.

Such amounts, while not revenue as defined in this Standard, are sometimes recognised in the statement of profit and loss appropriately.
Revenue from service transactions is usually recognised as the service is performed, either by the proportionate completion method or by the completed service contract method.

- **Proportionate completion method** — Performance consists of the execution of more than one act. Revenue is recognised proportionately by reference to the performance of each act. The revenue recognised under this method would be determined on the basis of contract value, associated costs, number of acts or other suitable basis. For practical purposes, when services are provided by an indeterminate number of acts over a specific period of time, revenue is recognised on a straight line basis over the specific period unless there is evidence that some other method better represents the pattern of performance.
Completed service contract method — Performance consists of the execution of a single act. Alternatively, services are performed in more than a single act, and the services yet to be performed are so significant in relation to the transaction taken as a whole that performance cannot be deemed to have been completed until the execution of those acts. The completed service contract method is relevant to these patterns of performance and accordingly revenue is recognised when the sole or final act takes place and the service becomes chargeable.
The Use by Others of Enterprise Resources Yielding Interest, Royalties and Dividends

The use by others of such enterprise resources gives rise to:

- **Interest**: Charges for the use of cash resources or amounts due to the enterprise
- **Royalties**: Charges for the use of such assets as know-how, patents, trade marks and copyrights
- **Dividends**: Rewards from the holding of investments in shares.

**Interest** accrues, in most circumstances, on the time basis determined by the amount outstanding and the rate applicable.

**Usually**, discount or premium on debt securities held is treated as though it were accruing over the period to maturity.
The Use by Others of Enterprise Resources Yielding Interest, Royalties and Dividends
(Contd.)

Royalties accrue in accordance with the terms of the relevant agreement and are usually recognised on that basis unless, having regard to the substance of the transactions, it is more appropriate to recognise revenue on some other systematic and rational basis.

Dividends from investments in shares are not recognised in the statement of profit and loss until a right to receive payment is established.

When interest, royalties and dividends from foreign countries require exchange permission and uncertainty in remittance is anticipated, revenue recognition may need to be postponed.
Effect of Uncertainties on Revenue Recognition

Recognition of revenue requires that revenue is measurable and that at the time of sale or the rendering of the service it would not be unreasonable to expect ultimate collection.

Where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, e.g., for escalation of price, export incentives, interest etc., revenue recognition is postponed to the extent of uncertainty involved.

In such cases, it may be appropriate to recognise revenue only when it is reasonably certain that the ultimate collection will be made. Where there is no uncertainty as to ultimate collection, revenue is recognised at the time of sale or rendering of service even though payments are made by installments.
Effect of Uncertainties on Revenue Recognition (Contd.)

When the uncertainty relating to collectability arises subsequent to the time of sale or the rendering of the service, it is more appropriate to make a separate provision to reflect the uncertainty rather than to adjust the amount of revenue originally recorded.

An essential criterion for the recognition of revenue is that the consideration receivable for the sale of goods, the rendering of services or from the use by others of enterprise resources is reasonably determinable. When such consideration is not determinable within reasonable limits, the recognition of revenue is postponed.

When recognition of revenue is postponed due to the effect of uncertainties, it is considered as revenue of the period in which it is properly recognised.
Main Principles

Revenue from sales or service transactions should be recognised when the requirements as to performance are satisfied, provided that at the time of performance it is not unreasonable to expect ultimate collection. If at the time of raising of any claim it is unreasonable to expect ultimate collection, revenue recognition should be postponed.

The amount of revenue from sales transactions (turnover) should be disclosed in the following manner on the face of the statement of profit and loss:

- Turnover (Gross)          XX
- Less: Excise Duty         (XX)
- Turnover (Net)            XX
The amount of excise duty to be deducted from the turnover should be the total excise duty for the year except the excise duty related to the difference between the closing stock and opening stock. The excise duty related to the difference between the closing stock and opening stock should be recognised separately in the statement of profit and loss, with an explanatory note in the notes to accounts to explain the nature of the two amounts of excise duty.
In a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been fulfilled:

- The seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and
- no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods
In a transaction involving the rendering of services, performance should be measured either under the completed service contract method or under the proportionate completion method, whichever relates the revenue to the work accomplished. Such performance should be regarded as being achieved when no significant uncertainty exists Revenue Recognition regarding the amount of the consideration that will be derived from rendering the service.
Revenue arising from the use by others of enterprise resources yielding interest, royalties and dividends should only be recognised when no significant uncertainty as to measurability or collectability exists. These revenues are recognised on the following bases:

- **Interest**: on a time proportion basis taking into account the amount outstanding and the rate applicable.
- **Royalties**: on an accrual basis in accordance with the terms of the relevant agreement.
- **Dividends from investments in shares**: when the owner’s right to receive payment is established.
In addition to the disclosures required by Accounting Standard 1 on ‘Disclosure of Accounting Policies’ (AS 1), an enterprise should also disclose the circumstances in which revenue recognition has been postponed pending the resolution of significant uncertainties.
CASE STUDIES
Case Study 1

Voltality Limited, is in the business of selling Air Conditioners. It had sold 15 AC’s to Realty Limited, as on March 30, 2013. Realty Limited, had requested the Company, that it will take the delivery of the AC’s after few days, as the building in which the AC’s are proposed to be installed, is still not fully completed.

Can Voltality Limited recognise the revenue for the year ended March 31, 2013?
Yes.

- Revenue should be recognised notwithstanding that physical delivery has not been completed so long as there is every expectation that delivery will be made. However, the item must be on hand, identified and ready for delivery to the buyer at the time the sale is recognised rather than there being simply an intention to acquire or manufacture the goods in time for delivery.

- Hence, Voltality Limited, shall recognise the revenue on the AC’s sold to Realty Limited during the year ended March 31, 2013.
Powers Ltd, is a company whose business is manufacturing and installing of water pump sets has during the year sold 30 pump sets to Hybrid Plantations Limited. As per the terms of sale, Hybrid Plantations Limited will inspect the units and confirm whether they are fit for acceptance.

The accountant of Powers Ltd says that revenue shall not be recognised until installation and inspection is completed.

Is he correct?
Case Study 2

Yes.

- Revenue should normally not be recognised until the customer accepts delivery and installation and inspection are complete. In some cases, however, the installation process may be so simple in nature that it may be appropriate to recognise the sale notwithstanding that installation is not yet completed (e.g. installation of a factory-tested television receiver normally only requires unpacking and connecting of power and antennae).

- Hence the accountant of Powers Limited is correct.
Gulmohor Ltd, is a Company manufacturing designer clothes. As per the industry norms, the company sends the clothes to various designers for putting them up in their boutique.

The Policy of the Company is that, it recognises revenue once the clothes are sent to designers. Is the revenue recognition policy correct?
Case Study 3

No.

• 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.

• The revenue shall be recognised only when the designers have accepted the clothes or not conveyed their rejection before elapse of a fixed time period.
Ayura Ltd, manufactures herbal creams and lotions. As this is a start up Company, the management wants to introduce a scheme of ‘money back if not completely satisfied’ for a period of one year.

The accountant wants your help as he not clear about the revenue recognition in compliance with AS 9.
In the case of retail sales offering a guarantee of “money back if not completely satisfied” it may be appropriate to recognise the sale but to make a suitable provision for returns based on previous experience.

Accordingly, Ayura Ltd, shall recognise revenue and it shall make suitable provisions for the returns.
Case Study 5

Agarbathi Ltd, is a company manufacturing incense sticks. It manufactures the same in its plant at Macherla and from there goods are sent to consignees who sell the goods on behalf of the Company.

At what juncture shall the revenue be recognised?
In case of consignment sales wherein 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.

Hence, Agarbathi Ltd, shall recognise the revenue when the goods are sold by the designated persons, as they are acting in their capacity as consignees.
Hebbal Auto Ltd, trades in two wheelers and other motor vehicles. Its business consists of selling and repurchasing the same at a later date.

Does this amount so received by Hebbal Auto Ltd on account of such trade be recognised as revenue?
Sale/repurchase agreements i.e. where seller concurrently agrees to repurchase the same goods at a later date

For such transactions that are in substance a financing agreement, the resulting cash inflow is not revenue as defined and should not be recognised as revenue.

Hence Hebbal Auto Ltd, shall not recognise the amount so received as revenue.
Case Study 7

Vasuki Ltd, is a event management Company, which conducts various events. During the year, the Company has entered into an understanding with the Arts College, for managing various events which take place during the year.

When shall the revenue be recognised by the Company?
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.

Hence Vasuki Ltd, shall recognise the revenue accordingly.
Iconik Financial services Ltd, provides various financial services including but not limited to maintenance of demat account, advising the clientele, studies/ analysis on scrips.

Mr. A, is a newly qualified Chartered Accountant, who is appointed as a Finance officer in Accounts Department. He seeks your help with regard to revenue recognition. Can you please help.
Case Study 8

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. The recognition of such revenue should therefore have regard to:

• (a) whether the service has been provided “once and for all” or is on a “continuing” basis;
• (b) the incidence of the costs relating to the service;
• (c) when the payment for the service will be received.
• Hence the revenue shall be recorded accordingly.
Lesson Summary