Regulators publish new global revenue accounting standard

by Richard Crump

29 May 2014

AFTER more than a decade of effort, regulators yesterday published a global accounting standard that will overhaul the way businesses record revenue on their books, allowing investors to better compare how much companies from countries around the world earn.

In a major step towards creating a converged set of international accounting rules, global standard setter the IASB and US counterpart FASB released a converged standard on the recognition of revenue from contracts with customers that will improve comparability of financial statements globally.

The core principle of the new common global standard, which replaces the fragmented set of rules by which companies in different industries booked their revenues differently, is for companies to recognise revenues in a way that shows the transfer of good and services to customers that reflects the payment to which the company expects to be entitled.

"The revenue recognition standard represents a milestone in our efforts to improve and converge one of the most important areas of financial reporting. It will eliminate a major source of inconsistency in GAAP, which currently consists of numerous disparate, industry-specific pieces of revenue recognition guidance," said Russell Golden, chairman of FASB.

"The issuance of this standard is a major first step, but it is not the end of the process. Through the transition resource group and a robust implementation period, the FASB and the IASB will work to ensure that reporting organisations are able to make a smooth transition to the new requirements," Golden added.

The new standard will also enhance disclosure about revenue, provide guidance for transactions that were not previously addressed comprehensively - such as service revenue and contract modifications - and improve guidance for multiple-element arrangements. Additionally, the guidance will add detail to IFRS requirements and make US GAAP less prescriptive in favour of a more principles-based approach to revenue recognition.

In order to recognise revenue under the new rules, known as IFRS 15, companies will need to follow a five step process which begins by matching the contract with a customer, identifying the performance obligations in the contract, determining the transaction price, which is then allocated to performance obligation with revenue recognised as each performance obligation is met.

According to members of the accountancy profession, the changes will be most keenly felt companies that offer complex bundles of goods and services or provide long-term service contracts - such as telecoms, construction, real estate and software companies.

"For some of these companies, the change may present a formidable logistical challenge. This will involve assessing the impact of the standard on all the company's revenue streams and determining what customers pay for each element of goods and services sold as packages. This can be a complicated task," said Nigel Sleigh-Johnson, head of the reporting faculty at ICAEW. "For many other businesses - such as those undertaking straightforward retail transactions - the standard will mean only limited change."

The new rules might also require changes to companies' systems and processes to collect the necessary data, experts said.

"It will have significant knock-on effects on the reporting of key performance indicators, for example, and may impact companies' internal systems.Companies should not underestimate the possible impact of the new standard either in terms of change in revenue profile and the potential need for changing systems, processes and disclosures," said Veronica Poole, Deloitte's global IFRS technical leader.

Brian O'Donovan, partner with KPMG's International Standards Group based in London, praised the joint standard as "a major achievement for the standard setters" but added that, for companies, the "real work is just beginning".

Companies using IFRS will need to apply the new standard for reporting periods beginning on or after 1 January 2017, though early adoption is allowed.

Hans Hoogervorst, chairman of the IASB commented: "The successful conclusion of this project is a major achievement for both boards. Together, we have improved the revenue requirements of both IFRS and US GAAP, while managing to achieve a fully converged Standard. Our attention now turns to ensuring a successful transition to these new requirements."