Revenue

1. An entity shall recognize revenue when:
   a) goods are sold or services are exchanged for similar goods or services
   b) goods are sold or services are exchanged for similar goods or services in a transaction that has commercial substance.
   c) goods are sold or services are exchanged for dissimilar goods or services in a transaction that has commercial substance.

2. An entity shall include in revenue:
   a) only the gross inflows of economic benefits received and receivable by the entity on its own account, including all amounts collected on behalf of third parties such as sales taxes, goods and services taxes and value added taxes.
   b) only the gross outflows of economic benefits paid and payable by the entity from its own account, including all amounts paid on behalf of third parties such as sales taxes, goods and services taxes and value added taxes.
   c) only the gross outflows of economic benefits paid and payable by the entity from its own account, excluding all amounts paid on behalf of third parties such as sales taxes, goods and services taxes and value added taxes.
   d) only the gross inflows of economic benefits received and receivable by the entity on its own account, excluding all amounts collected on behalf of third parties such as sales taxes, goods and services taxes and value added taxes.

3. An entity shall measure the revenue transaction at:
   a) the fair value of the goods or services received adjusted by the amount of any cash or cash equivalents transferred.
   b) the present value of the goods or services given up adjusted by the amount of any cash or cash equivalents transferred.
   c) the acquisition cost of the goods or services given up adjusted by the amount of any cash or cash equivalents transferred.

4. An entity shall measure the revenue from transaction involving the rendering of services and construction contracts
   a) by reference to the percentage of completion method applied at the end of the reporting period.
   b) by reference to the effective interest rate method applied at the end of the reporting period.
   c) by reference to the discounting method applied at the end of the reporting period.

<u>Example 1: revenue from the sale of goods</u>

A manufacturer sells one of its products for CU500 per unit.

a) However, the manufacturer gives customers a 20 per cent discount on orders of 100 units or more. A customer buys 100 units in a single order.

b) However, the manufacturer gives customers a 20 per cent discount on orders of 100 units or more. Furthermore, when the customer has purchased 1,000 or more units in a single annual financial reporting period, the retailer awards the customer a further volume discount of 10 per cent of the list price for all units acquired by the customer in that financial year. A customer buys 100 units of the product each month for one annual financial reporting period.

c) A manufacturer sells its product on credit. To encourage early settlement the retailer awards its customers a 10 per cent early settlement discount provided that the customer settles within 30 days of buying the goods. Normal credit terms are 60 days. Customer 1 pays within 30 days of the date of purchase to settle the amount owing for 90 units bought from the entity. Customer 2 pays within, 60 days after the date of purchase, to settle the amount owing for 90 units bought from the entity.

What is the recognized amount of revenue in each of the presented above cases?

<u>Example 2: revenue from rendering of services</u>

A law firm is contracted to represent a group of past employees in a class action lawsuit against a mining company.

a) The law firm will receive a fee for legal services provided equal to 20 per cent of the total damages awarded by the court (or any out of court settlement). However, if the lawsuit fails the law firm will receive nothing.

b) Irrespective of the outcome of the lawsuit the law firm will be remunerated on the basis of the time spent in pleading the case (ie X hours spent × CU100 per hour). In the current reporting period the law firm spent 120 hours on the lawsuit.

What is the amount of revenue recognized by a law firm in both cases?

<u>Example 3: revenue from rendering of services</u>

A calibration engineer entered into a contract to calibrate a manufacturer's machine at six-month intervals over a two-year period ending 31 December 20X2. On 1 January 20X1 the manufacturer paid the calibration engineer CU10,000. The cost to the calibration engineer of performing each calibration is approximately CU1,000.

What is the amount of revenue recognized at 31 December 20X1?

<u>Example 4: revenue from rendering of services</u>

An entity provides maintenance services to a third party under a contract for a fixed price of CU100,000. The entity initially estimated that its total costs under the contract will be CU60,000. At the end of the reporting period (20X1) the entity has incurred CU50,000 costs and it expects to incur a further CU15,000 costs to complete the maintenance services.

The entity determines the stage of completion of the contract by reference to the proportion that costs incurred for work performed to date bear to the estimated total costs.

What is the amount of revenue recognized at the end of the reporting period 20X1?

<u>Example 5: revenue from rendering of services</u>

A security firm enters into contracts to provide armed responses to homeowners when their alarm systems are triggered. The security firm has a 30 June year-end. On 1 January 20X1 one homeowner paid the security firm CU10,000. In return for the fixed fee, the security firm is contractually obliged to provide its armed response services to the homeowner for a two-year period.

What is the amount of revenue recognized at the end of each reporting period during the lifetime of the contract?

<u>Example 6: revenue from rendering of services</u>

A vehicle dealer enters into contracts to maintain its customer's new vehicle for a three-year period.

On 1 January 20X1 a customer paid the dealer CU10,000. Experience has shown that the costs to the dealer of maintaining new vehicles of the model owned by the customer are on average CU1,000 in the first year of ownership, CU1,000 in the second year and CU3,000 in the third year.

What is the amount of revenue recognized at the end of each reporting period during the lifetime of the contract?

<u>Example 7: revenue from construction contracts</u>

Under a construction contract, a contractor agrees to a fixed contract price of CU2,000 to refurbish the kitchen of a residential flat. The contractor's initial estimate of contract costs at 1 February 20X1, the date the contract is agreed, is CU1,200. The contract price will be paid to the contractor on completion of the refurbishment. The refurbishment was completed on 31 July 20X1 at a cost of CU1,250 (i.e. actual costs incurred under the contract as at 31 July 20X1 are CU1,250).

a) The contractor has a 31 December year-end.
b) The contractor has a 30 June year-end. As at 30 June 20X1 contract costs incurred for work performed to date are CU800 and the contractor estimates that costs to complete the contract will be CU400 (i.e. total contract costs will be CU1,200). The contractor determines the stage of completion of the contract by calculating the proportion that contract costs incurred for work performed to date bear to the latest estimated total contract costs.

What is the amount of revenue recognized at the end of each reporting period during the lifetime of the contract in each of the presented above cases?

Example 8: revenue from construction contracts

Under a construction contract, a contractor agrees to receive a 40 per cent fixed return on its direct contract costs from the customer. The contractor's initial estimate of contract costs at 1 January 20X1, the date the contract is agreed, is CU2,000 (all of which are considered direct costs). Therefore, expected revenue under the contract is CU2,800. The contract is expected to last two years. The contractor has a 31 December year-end.

At 31 December 20X1 contract costs of CU1,045 have been incurred and the contractor expects total contract costs to be CU1,900 (all considered direct costs). At 31 December 20X2 actual costs are CU2,000. However, only CU1,800 meet the criteria in the contract to be considered direct costs when determining the 40 per cent fixed return.

The contractor determines the stage of completion of the contract by calculating the proportion that contract costs incurred for work performed to date bear to the latest estimated total contract costs.

What is the amount of revenue recognized at the end of each reporting period during the lifetime of the contract?

Income tax

1. Income tax consists of:
   a) domestic taxes that are based on taxable profits.
   b) foreign taxes that are based on taxable profits.
   c) taxes that are payable by a subsidiary, associate or joint venture on distributions to the reporting entity.
   d) all of the above.

2. Decide in which order individual procedures which are presented below should take place while accounting for a deferred tax (the first four steps of the deferred tax methodology)

(i) Compute any temporary differences, unused tax losses and unused tax credits.

(ii) Determine the tax basis at the reporting date of all those assets and liabilities, and of other items that have a tax basis.

(iii) Recognize deferred tax assets and liabilities arising from the temporary differences, unused tax losses and unused tax credits.

(iv) Identify which assets and liabilities are expected to affect taxable profit if they were recovered or settled for their carrying amount.

   a) (i), (ii), (iii), (iv).
   b) (iv), (ii), (i), (iii).
   c) (ii), (iv), (i), (iii).
   d) (ii), (i), (iii), (iv).

3. Decide which statements are true:
   a) An entity shall recognize a current tax liability for tax payable on taxable profit for the current and past periods.
   b) An entity shall measure a current tax liability (asset) at the amounts it expects to pay (recover) using the tax rates and laws that have been enacted or substantively enacted by the reporting date.
   c) An entity shall not recognize changes in a current tax liability or current tax asset.
   d) An entity shall not include in the amounts recognized the effect of the possible outcomes of a review by the tax authorities.

4. Deferred tax arises from:
   a) the difference between the amounts recognized for the entity's assets and liabilities in the statement of financial position and the recognition of those assets and liabilities by the tax authorities, and the carryforward of currently unused tax losses and tax credits.

b) the difference between the amounts recognized for the entity's assets and liabilities in the statement of financial position and the recognition of those assets and liabilities by the tax authorities.
c) the difference between the amounts which were recognized by an entity and which were paid by an entity in current and past periods.

<u>Example 1: current tax</u>

An entity has a year-end of 31 March. The tax year in the jurisdiction runs from 1 April to 31 March. The relevant income tax rate for 20X7/20X8 is 15 per cent. The entity has an accounting profit of CU150,000 for the year ended 31 March 20X8. The rules determining the determination of taxable profit in the jurisdiction are identical to the IFRS for SMEs for the year ended 31 March 20X8, except for the following income and expenses:

- CU20,000 royalty revenue recognized in 20X8 is exempt from income tax.
- No tax deduction is permitted for entertainment expenses of CU5,000.
- No tax deduction for bad debts is allowed until the debtors are derecognized from the financial statements. The bad debt provision, which is offset against trade receivables, was CU4,000 on 31 March 20X7 and CU4,500 on 31 March 20X8.
- The building is depreciated at a faster rate for tax purposes. The amount of tax depreciation deductible in the year ended 20X8 was CU43,000. The amount of accounting depreciation in the financial statements for the same building for the year was CU35,000.

The deferred tax impact of the transactions above is ignored in this question. What is the recognized amount of current income tax?

<u>Example 2: current tax</u>

An entity calculates its taxable profit to be CU100,000 for the tax year 20X7/20X8 determined in accordance with the relevant tax rules in its jurisdiction. The tax year in the jurisdiction runs from 1 April to 31 March. The appropriate income tax rate for 20X7/20X8 is 20 per cent.

a) The current tax payable for the tax year 20X7/20X8 is payable by 30 September 20X8 and the entity makes the payment on 15 September 20X8. The entity has a 31 March financial year end (end of the reporting period).
b) On 1 June 20X8, before the financial statements are authorised for issue, the entity recalculates its taxable profit to be CU95,000 owing to new information arising between 31 March and 1 June 20X8 that provides evidence of conditions that existed at 31 March 20X8 (eg because the amount of profit-sharing payments to employees for the year ended 31 March 20X8, which had originally been estimated, is now finalised).

What is the recognized amount of current income tax in both cases? How should it be accounted for?

Example 3: carryback for current tax loss

In accordance with the relevant tax rules in its jurisdiction, an entity estimates its taxable loss for the tax period 20X7/20X8 at CU9,000. The tax legislation in the jurisdiction permits entities to carry back losses three tax years into the past. Taxable income in 20X6/20X7 was CU7,000, in 20X5/20X6 it was CU5,000 and in 20X4/20X5 it was CU3,000. The entity has a 30 September financial year-end (end of the reporting period) and this coincides with the entity's tax year. The relevant income tax rates are as follows:

- 18 per cent in 20X6/20X7 and 20X7/20X8
- 20 per cent in 20X5/20X6
- 17 per cent in 20X4/20X5.

What is the recognized amount of carryback for current tax loss if:

a) The tax legislation in the jurisdiction permits entities to carry back losses three tax years into the past and there is no requirement on which of the three years the loss is set off against first.
b) The tax legislation in the jurisdiction permits entities to carry back losses three tax years into the past and there is a requirement that the entity should set the losses against the most recent period possible, i.e. 20X6/20X7 first, 20X5/20X6 second and 20X4/20X5 last.

Example 4: deferred tax

An entity has an item of equipment that is depreciated faster for tax purposes than for financial reporting purposes. On 31 December 20X1 a temporary difference of CU1,000 arises related to this equipment that is expected to increase taxable profit in the future. The temporary difference is expected to reverse in five years' time. In the entity's jurisdiction, tax is payable at 20 per cent on the first CU100,000 of taxable profit earned, 25 per cent on the next CU200,000 of taxable profit earned, 30 per cent on the next CU200,000 of taxable profit earned, and 35 per cent on any remainder (ie excess above CU500,000). In 20X6 the entity expects to earn taxable profit of CU650,000.

What is the recognized amount of differed tax liability?