Ind AS
Worked Example

Revenue Recognition:
Measuring Progress using the Output Method

Worked Example

Recognition of Revenue over time: Measuring progress using the Output Method

SCENARIO

The reporting period of ABC Ltd ends on 31 March every year. On 1 October 20x3, ABC Ltd entered into a construction contract for a fixed price of CU 25,000, which was expected to be completed on 31 December 20x5. The estimated cost to complete the contract was CU 11,000. An item of machinery was used in the contract from 1 January 20x4 and was expected to be used till the completion of the contract. The total depreciation of the item of machinery for this 2-year period was CU 8,000. ABC Ltd decided to allocate the depreciation using the straight line method (SLM). ABC Ltd decided that the percentage of completion was to be calculated as the agreed value of work completed as a percentage of the agreed contract price.

The following information was provided for the reporting period ended on 31 March –

	20x4	**20x5**
	CU	**CU**
Agreed value of work certified	7,000	16,250
Costs incurred to-date (excluding depreciation)	5,000	9,600
Progress payment received	6,000	9,000
Estimation of work completed	35%	75%

WHAT THE STANDARD SAYS

As per Ind AS 115, an entity should recognise revenue over time by measuring the progress towards complete satisfaction of that performance obligation. The objective when measuring progress is to depict an entity's performance in transferring control of goods promised to a customer (ie, the satisfaction of an entity's performance obligation). The appropriate method that ABC Ltd used to measure progress towards complete satisfaction of the performance obligation is the *output method*. The output method recognises revenue on the basis of direct measurements of the value to the customer of the goods transferred to date relative to the remaining goods promised under the contract.

	CU
Total value of the contract	25,000
Total expected costs to be incurred (CU 11,000 + CU 8,000)	19,000
Expected profit	**6,000**

Total depreciation for the contract period is CU 8,000. The allocation of depreciation under SLM will be as under –

For the reporting period ended 31 March 20x4 – CU 8,000 ÷ 2 x 3/12 = CU 1,000

For the reporting period ended 31 March 20x5 – CU 8,000 ÷ 2 = CU 4,000

For the reporting period ended 31 March 20x6 – CU 8,000 ÷ 2 x 9/12 = CU 3,000

For the reporting period ended 31 March 20x4

Under the output method, the percentage of completion of contract is 28% (CU 7,000 ÷ CU 25,000 x 100)

Journal

1.	Receivable	CU 7,000	
	Revenue		CU 7,000
2.	Cash	CU 6,000	
	Receivable		CU 6,000
4.	Contract asset	CU 1,750 [7% (35% – 28%) x CU 25,000]	
	Contract liability		CU 1,750

Balance Sheet (Extract)

Assets	**CU**
Current assets	
Contract asset	1,750
Receivable (CU 7,000 – CU 6,000)	1,000
Equity	
Retained earnings	1,680
Liabilities	
Contract liability	1,750

Statement of Profit and Loss (Extract)

	CU
Revenue	7,000
Cost of sales (28% of CU 19,000)	5,320
Profit	**1,680**

For the reporting period ended 31 March 20x5

Under the output method, the percentage of completion of contract is 65% (CU 16,250 ÷ CU 25,000 x 100)

Journal

1.	Receivable (CU 16,250 – CU 7,000)	CU 9,250	
	Revenue		CU 9,250
2.	Cash	CU 9,000	
	Receivable		CU 9,000
4.	Contract asset	CU 750 [{10% (75% – 65%) x CU 25,000} – CU 1,750]	
	Contract liability		CU 750

Balance Sheet (Extract)

Assets	**CU**
Current assets	
Contract asset (CU 1,750 + CU 750)	2,500
Receivable (CU 1,000 + CU 9,250 – CU 9,000)	1,250
Equity	
Retained earnings	2,220
Liabilities	
Contract liability (CU 1,750 + CU 750)	2,500

Statement of Profit and Loss (Extract)

	CU
Revenue (CU 16,250 – CU 7,000)	9,250
Cost of sales [(65% of CU 19,000) – CU 5,320	7,030
Profit	**2,220**