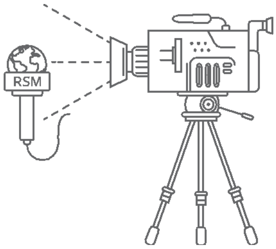
Wake Up Call

RSM

Revenue from contracts with customers



ED PSAK 72 specifies the accounting treatment for all revenue arising from contracts with customers. It replaces all existing PSAK dealt with revenue recognition. The core principle in ED PSAK 72 is that an entity will recognize revenue at an amount reflects the consideration to which the entity expects to be entitled in exchange for transferring goods or services to a customer.

Revenue is always an interesting subject in accounting and auditing. In many cases, revenue recognition becomes a way for cooking the book. Different industry has unique characteristics that may lead to different revenue recognition. Currently there are several accounting standards for revenue recognition, those are PSAK 23: Revenue, PSAK 34: Construction Contracts, ISAK 10: Customer Loyalty Programmers, ISAK 21: Agreements for the Construction of Real Estate, ISAK 27: Transfer of Assets from Customers, and PSAK 44: Accounting for Real Estate Development Activities.

Those standards are used by entities in various industries to treat their revenues in accounting records. Unfortunately, there are inconsistencies and weaknesses in the current standards. For example, PSAK 23 defines the criteria for revenue recognition is a principle -based standard. While PSAK 44 set rules for revenues recognition that is a rule-based standard. In addition, current standards have a limited guidance on important topics such as revenue recognition for multiple element arrangements. This is one of the reasons for the Indonesian accounting standard setters to issue ED PSAK 72: Revenue from contracts with customers. The ED PSAK 72 is intended to replace all those standards mentioned above.

ED PSAK 72 specifies the accounting treatment for all revenue arising from contracts with customers. This standard applies only for contract that have commercial substance, which is expected to change as a result of the contract (I-e-risk, timing, cash flow) According to ED PSAK 72, there are five basic steps that an entity needs to follow. First, an entity must identify the contract, or contracts, to deliver goods and services to customers. Any contracts – written, oral or implied by the entity's business practice – that create enforceable right and obligation is within the scope of the standard (ED PSAK-72). Second, an entity must identify the promised goods and services within the contract and determine which of those goods and services are separate, or distinct, performance obligation. The performance obligations identified in a contract with a customer may not be limited to goods or services explicitly stated in that contract. A contract with a customer may also include promises that are implied by an entity's customary business practices, published policies or specific statements.

The third step, is that an entity shall consider the terms of contract and its customary business practices to determine the transaction price. Transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer. Fourth, an entity allocates the transaction price to the performance obligation in the contracts. Allocation is generally done in proportion to the stand-alone selling price. And finally, an entity only recognizes revenue when it satisfies an identified performance obligation by transferring a promised goods or services to a customer. Goods or services are generally considered to be transferred when the customer obtains control. Please note that recognizing revenue upon a transfer of control is a different notion from the risks and rewards model that currently adopted in PSAKs.

These five steps will likely affect entity's financial statements, business process and internal controls over financial reporting. For instance, the entity's business process must accommodate the need of identifying performance obligation arising from promises, even it is only implied. Similarly, internal control also must able to prevent from misidentify such performance obligation. However the impact will vary. Some entity may be able to implement with limited effort. Others may need significant efforts.

KEY POINTS

- Current standard on revenue contains inconsistencies and weaknesses.
- Proposed standard, ED PSAK 72, aims to replace and improve the currents.
- Proposed new standard will affect entity's financial statements, business process and internal controls over financial reporting.