

PART A Suggested Solution DCS

Describe how the revenue in the contract between DCS and PHD will be recognised and measured. You may assume that the contract between the parties is within the scope of IFRS 15. (<i>Required assumed IFRS15 contact, therefore you do not need to Identify the contract?</i>)		
Identifying the performance obligations		
There are five distinct performance obligations in the contract.		
<u>The supply of licence to the computer software; installation and interface services; managing the computer systems and providing production development support.</u>	2	
The supply of licence to the inventory control software <u>is capable of being distinct as PHD can benefit from the software (IFRS 15 par 27a) together with installation and interface services which is sold separately by DCS or any software expert and the installation and interface does not significantly modify the software (IFRS15 par 29 b).</u>	1	
The supply of the licence to the inventory control system is also <u>separately identifiable</u> from the other promises in the contract as this is <u>distinct from the obligation to install and create an interface in the contract</u> and is <u>separate from the obligations to manage PHD's computer systems and provide production development support</u> as these are not interrelated or highly dependent on each other (IFRS 15 par 29 c).	1	
Both the computer services and production development support to be supplied by DCS are <u>each capable of being distinct</u> as PHD benefits from these services independently from the licence to use the software and its installation (IFRS 15 par 28) <u>and are each separately identifiable</u> from other promises in the contract <u>and are not interrelated or highly dependent on either the licence to use the software or any other services promised in the contract (IFRS 15 par 29c).</u>	1	
Allocation of the transaction price to performance obligations.		
IFRS 15 par 73, 74 and 76 require that the transaction price must be allocated to each distinct performance obligation <u>based on the stand-alone selling price at which the entity would sell the goods or service separately to a customer.</u>	1	
The performance obligations include the obligation to <u>provide production support for which there is no observable selling price as this is a new category of service for which DCS has not yet established a price</u> IFRS 15 par 79 (c) (ii).	1	
Therefore in compliance with IFRS 15 par 79 (c) the <u>residual approach</u> may be used to estimate the stand-alone selling price of this component of the contract by deducting the sum of the stand-alone selling prices of all the other promised goods or services in the contract from the total transaction price.	1	
The total contract price would be allocated as follows:		
Computer software	530*550/610	\$ 477 870
Installation and interface	530*60/610	\$52 130
Managing computer systems		\$5 400 000
Production development fee		\$230 400
		\$6 160 400
Revenue recognition		

In accordance with IFRS 15 par 31 revenue is recognised when the entity satisfies a performance obligation by transferring goods or services to customer. An asset is transferred as the <u>customer gains control of the asset</u> . Revenue of \$477 870 will be recognised when DCS transfers the licence to use the software to PHD , \$52 130 in respect of the installation and supply the computer software, and the interface to the existing accounting package is recognised at the point in time when the installation is complete. Management and production support services are transferred and consumed over time (par 35 a) and monthly revenue of \$156 400 is recognised.	1 1 1 1
Presentation	23 Max 19 1 Total 20

PART B

Refurbishment costs	
The refurbishment costs do not meet the definition of a provision as there is no past event that gives rise to a present obligation to refurbish the taxi fleet.	1
When the taxis were initially recognised, the cost of each significant component should have been recognised separately and depreciated over its useful life IAS 16 par 44.	1
Because the interior of the taxis have a life of 3 years as compared to the expected 5 year life of the body the interior and the body are significant components and should be recognised separately.	1
The interior would be depreciated over three years and the body over five years.	1
The cost of the refurbishment, \$500 000, would be recognised as a new component when incurred and depreciated over its expected life of 2 years.	1 1
	6 marks

Contract cancellation costs	
The contract cancellation costs are not a liability of Gilbert at acquisition date . Gilbert does not have the obligation to pay the settlement amount. This is Egbert's obligation arising from its decision to cancel the supply contracts.	1
The present obligation will arise in Egbert when they confirm with the suppliers that they will be cancelling the contact, the past event, and commit to paying the cancellation fee which gives rise to the present obligation.	1
Therefore the liability will need to be reversed against goodwill and non-controlling interest and recognised as an obligation in Egbert's' records when the contracts are cancelled.	2 1

The liability must be measured at its present value at initial recognition as it is payable over two years and must be remeasured to its present value at the end of the year.	1 1
Finance charges will be recognised in the income statement.	1
	8 marks Max 7 marks

Investment in Dilbert debentures	
It is inappropriate to classify the debentures in Dilbert as a financial asset measured at amortised cost in terms of IFRS 9 par 4.1.2.(b) because the cash flows on the debentures are not solely payments of the principal and interest. The coupon on the principal has been reduced to take into account the holder's option to convert the debentures into shares.	1 1 1
The investment in debentures should have been classified at fair value through profit and loss.	1
The debenture is a hybrid contract because it confers on Eggbert the contractual right to receive the principal and interest and a call option to demand shares in Dilbert.	1
Because the hybrid instrument contains a host that is an asset within the scope of IFRS 9 the entire contract must be classified at fair value through profit and loss because it fails to meet the amortised cost criteria.	1
Therefore the recognised interest received must be reversed and the asset must be remeasured to fair value through profit and loss.	1 1
	8 marks

Accounts Receivable	
IFRS 9 par 5.5.1 requires that an entity recognises a loss allowance for financial assets measured at amortised cost. In addition par 5.5.15 requires that the loss allowance on accounts receivable that do not include a significant financing component must be measured at an amount equal to lifetime expected credit losses, defined as the expected losses from all possible default events over the expected life of a financial instrument.	1 1 1
The basis that Eggbert has applied to measure the loss allowance, i.e. a provision matrix, is recognised as a practical expedient in IFRS 9 par B5.5.35. However, as Eggbert's credit term is 90 days a credit loss allowance should be recognised for amounts outstanding between 90-180 days.	1 1
Therefore the existing allowance for irrecoverable amounts must be revised to include a credit loss allowance on balances outstanding between 90-180 days and balances outstanding before 90 days must be assessed for possible defaults.	1 1

Because the accounts receivable balances are expected to be paid within a year of the reporting date the time value of money need not be taken into account.	1
	8 marks
Presentation	1
	30 marks