PHILIPPINE INTERPRETATIONS COMMITTEE (PIC)
QUESTIONS AND ANSWERS (Q&As)

<u>Q&A No. 2020-04 (Addendum to PIC Q&A 2018-12-D)</u>

PFRS 15 - Step 3 - Requires and Entity to Determine the Transaction Price for the Contract

Issue

Would a mismatch between the Percentage-of -Completion (POC) and schedule of payments constitute a significant financing component in determining the transaction price given the following scenarios:

i. Higher payment (buyer pays ahead of the POC); and
ii. Lower payment (percentage of completion is ahead of the buyer's payment).

Background

Please refer to the case facts in PIC Q&A No. 2018-12-D issued last February 14, 2018.

Consensus

In reference to PFRS 15.62(c), there is no significant financing component, if the difference between the promised consideration and the cash selling price of the good or service (as described in paragraph 61) arises for reasons other than the provision of finance to either the customer or the entity, and the difference between those amounts is proportional to the reason for the difference.

The support should be documented in writing, by the real estate entity, considering both qualitative and quantitative factors.

Examples of scenarios or payment schemes where there maybe no significant financing components are as follows:

a) Upfront payment of full cash price with discount - the contract to sell has no SFC, if the amount of discount generally corresponds to the amount of the savings on inventory holding costs and selling costs which the real estate developer shares with the customer.
b) Other real estate sale payment schemes that might provide the entity or the customer with protection from the other party failing to adequately complete some or all of its obligations under the contract.

Also, as provided under paragraph 63 of PFRS 15, an entity need not adjust the promised amount of consideration for the effects of a significant financing component if the entity expects, at contract inception that the timing difference of the receipt of full payment of the contract price and that of the completion of the project, are expected within one year and SFC is not expected to be significant.

Transition and Effective Date

The consensus in this Q&A is effective from the date of approval of the FRSC and will follow the transition provision of the previously issued PIC Q&A.

Date approved by PIC: November 6, 2020

PIC Members

Wilson P. Tan, Chairman

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Date approved by FRSC: **November 11, 2020**

REFERENCES

PFRS 15.61
The objective when adjusting the promised amount of consideration for a significant financing component is for an entity to recognize revenue at an amount that reflects the price that a customer would have paid for the promised goods or services if the customer had paid cash for those goods or services when (or as) they transfer to the customer (i.e. the cash selling price). An entity shall consider all relevant facts and circumstances in assessing whether a contract contains a financing component and whether that financing component is significant to the contract, including both of the following:

(a) the difference, if any, between the amount of promised consideration and the cash selling price of the promised goods or services; and

(b) the combined effect of both of the following:
   (i) the expected length of time between when the entity transfers the promised goods or services to the customer and when the customer pays for those goods or services; and
   (ii) the prevailing interest rates in the relevant market.

PFRS 15.62
Notwithstanding the assessment in paragraph 61, a contract with a customer would not have significant financing component if any of the following factors exist:

(a) the customer paid for the goods or services in advance and the timing of the transfer of those goods or services is at the discretion of the customer.

(b) a substantial amount of the consideration promised by the customer is variable and the amount or timing of that consideration varies on the basis of the occurrence or non-occurrence of a future event that is not substantially within the control of the customer or the entity (for example, if the consideration is a sales-based royalty).

(c) the difference between the promised consideration and the cash selling price of the good or service (as described in paragraph 61) arises for reasons other than the provision of finance to either the customer or the entity, and the difference between those amounts is proportional to the reason for the difference. For example, the payment terms might provide the entity or the customer with protection from the other party failing to adequately complete some or all of its obligations under the contract."

PFRS 15.63
As a practical expedient, an entity need not adjust the promised amount of consideration for the effects of a significant financing component if the entity expects, at contract inception, that the period between when the entity transfers a promised good or service to a customer and when the customer pays for that good or service will be one year or less.