

Background

The following is an extract from the statement of financial position of Fiskerton, a public limited entity as at 30 September 20X8.

	\$'000
Non-current assets	160,901
Current assets	110,318
Equity share capital (\$1 each)	10,000
Other components of equity	20,151
Retained earnings	70,253
Non-current liabilities (bank loan)	50,000
Current liabilities	120,815

The bank loan has a covenant attached whereby it will become immediately repayable should the gearing ratio (long-term debt to equity) of Fiskerton exceed 50%. Fiskerton has a negative cash balance as at 30 September 20X8.

Halam property

Included within the non-current assets of Fiskerton is a property in Halam which has been leased to Edingley under a 40-year lease. The property was acquired for \$20 million on 1 October 20X7 and was immediately leased to Edingley.

The asset was expected to have a useful life of 40 years at the date of acquisition and have a minimal residual value. Fiskerton has classified the building as an investment property and has adopted the fair value model.

The property was initially revalued to \$22 million on 31 March 20X8. Interim financial statements had indicated that gearing was 51% prior to this revaluation. The managing director was made aware of this breach of covenant and so instructed that the property should be revalued. The property is now carried at a value of \$28 million which was determined by the sale of a similar sized property on 30 September 20X8. This property was located in a much more prosperous area and built with a higher grade of material. An independent professional valuer has estimated the value to be no more than \$22 million. The managing director has argued that fair values should be referenced to an active market and is refusing to adjust the financial statements, even though he knows it is contrary to international accounting standards.

Sales contract

Fiskerton has entered into a sales contract for the construction of an asset with a customer whereby the customer pays an initial deposit. The deposit is refundable only if Fiskerton fails to complete the construction of the asset. The remainder is payable on delivery of the asset. If the customer defaults on the contract prior to completion, Fiskerton has the right to retain the deposit. The managing director believes that, as completion of the asset is performed over time, revenue should be recognised accordingly. He has persuaded the accountant to include the deposit and a percentage of the remaining balance for construction work in revenue to date.

Required:

(b) In accordance with International Financial Reporting Standard (IFRS®) 15 Revenue from Contracts with Customers, discuss whether revenue arising from the sales contract should be recognised on a stage of completion basis. (4 marks)