



Solution 90.1

Component	Sales revenue
Index	Initial recognition
Short title	Reliable measurement of costs incurred

Attention: This guidance is based on the revised standards and interpretations that are mandatory for accounting periods commencing 1 January 2005. A company may early adopt an individual revised standard, but only in its entirety. Guidance based on the previous version of the standards is included in the “Applying IFRS 2004” guidance.

Issue

An entity should recognise revenue when **[IAS18R.14(a)-(e)]**:

- a) the entity has transferred significant risks and rewards of ownership of the goods to the buyer;
- b) the entity does not retain continuing managerial involvement or control over the goods sold;
- c) the amount of revenue can be measured reliably;
- d) it is probable that the economic benefits associated with the transaction will flow to the entity; and
- e) the costs incurred or to be incurred in respect of the transaction can be measured reliably.

How should management recognise revenue in respect of a sale of equipment for which a warranty has been given but for which no prior experience of warranty costs is available?

Background

Entity A has developed a new engine based on the principles of perpetual motion. Long-term testing of the engine has not been possible because the technology is so new. However, the sale of the first such engine has been agreed, and a one-year warranty for parts and labour has been provided.

Management is unable to assess the expected costs of the warranty, but was prepared to provide the warranty in order to obtain the first sale.

Solution

Management should not recognise revenue in respect of the engine sale until the one-year warranty period has expired. Management is not able to assess the likely total cost of the sale, and accordingly does not meet the revenue recognition criteria in respect of reliable measurement of the costs of the sale.