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PwC Alert

The new revenue standard is here. How will it affect automotive companies?

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The new framework for revenue recognition is here.

On 2 September 2014, the Malaysian Accounting Standards Board issued MFRS 15 *Revenue from Contracts with Customers*. This standard is word for word that of IFRS 15 issued by the International Accounting Standards Board. Entities are required to apply MFRS 15 for annual periods beginning on or after 1 January 2017. Early adoption is permitted.

The new revenue standard will replace all existing revenue recognition guidance under IFRS, MFRS and FRS.

This standard will affect many companies, but those most significantly impacted are likely to be companies with a longer delivery cycle, complex contract terms, and goods and services that come as a package.

Before diving into the financial reporting implications - which can be significant - consider the strategic ones. This means looking across the business, which could require input from business unit heads, operations, sales, legal, HR, finance, tax, and IT. This cross functional team can evaluate how revenue recognition affects each function and the business as a whole.

Automotive companies should start reviewing existing revenue arrangements, contract terms, and business practices, to identify where changes might occur:
- Will you have to rethink customer negotiations?
- What might compensation and benefit plans look like in the future?
- Should you rethink how you sell your products?
- What do you need to communicate to your investors, and when?
- Are there business opportunities resulting from increased flexibility?

Why change?

The objective of MFRS 15 is to provide one comprehensive revenue recognition model for all contracts with customers to improve comparability within industries, across industries, and across capital markets.

Preparing for the impending change

"While many companies can afford to wait until closer to the 2017 effective date, those who are significantly affected, such as automotive companies, will need to start now to get the necessary systems changes up and running in time."

Two adoption methods

(1) Full retrospective method
Companies can choose how they want to adopt the new standard. One way is by recasting prior period financial statements as if the guidance had always existed, which may require a lot of time and effort.

(2) Simplified transition method
Companies can instead choose to apply the new guidance prospectively and show the numbers in the year of adoption under both the new and old model. For example, this method requires presenting the 2017 financial statements under the new guidance, but including a footnote disclosure of all financial statement line items and the amounts they would have been under legacy guidance for 2017. This method offers a simpler alternative, but it isn't without its challenges.

Manage the transition

Transition could be especially difficult for companies with multi-year contracts. Start record keeping soon if retrospective application is a consideration. Do a cost-benefit analysis: Do you have the resources at hand to do one method more effectively than the other? Is there a benefit to your business in having comparability between the before-and-after? What do your investors expect? What are your competitors doing?

Plan for adoption

Your plan for adoption should include forming a cross-functional steering committee that oversees the entire process and takes into consideration the impact on your business as a whole.

Take inventory of arrangements that may be impacted and identify the gaps in your systems and controls before deciding on an implementation plan.

(See Appendix (page 18) for key areas and activities to consider in your implementation plan)

1 Develop — a plan to communicate to stakeholders

2 Consider — changes to strategies and contract terms

3 Identify — gaps in system and controls

4 Strategise — affected contract provisions

5 Form — a cross-functional steering committee

The core principle: a new

The core principle of MFRS 15 is that revenue is recognised when the goods or services are transferred to the customer, at the transaction price. Revenue is recognised in accordance with that core principle by applying a 5-step model.

Step 1	Step 2	Step 3	Step 4	Step 5
Identify the contract	Separate performance obligations	Determine transaction price	Allocate transaction price	Recognise revenue

Step 1: Identify contract(s) with customer

A contract creates enforceable rights and obligations. It may be written, verbal, or implied by customary business practice. Combine contracts when they are entered into at or near the same time and are negotiated as a package, payment of one depends on the other, or goods/services promised are a single performance obligation. Specific guidance about contract modifications prescribed to account for modifications as a separate contract or continuation of the original contract prospectively or with cumulative catch-up.

Step 2: Identify separate performance obligations in the contract(s)

Performance obligations are promises in a contract to transfer goods or services, including those a customer can resell or provide to its customer. Use the model's indicators to separate the performance obligations if they are capable of being distinct and if they are distinct based on the context of the contract (separately identifiable from other promises in the contract).

5-step model

Step 3: Determine the transaction price

Transaction price is the amount of consideration an entity is entitled to receive in exchange for transferring goods or services to customers. Determining the transaction price is straightforward when the contract price is fixed; it becomes more complex when it is not fixed. Discounts, rebates, refunds, credits, incentives, performance bonuses, and price concessions could cause the amount of consideration to be variable. In situations where there are variable considerations, transaction price is estimated based on the expected value or the most likely amount but is constrained up to the amount that is highly probable of no significant reversal in the future. The minimum amount that meets this criteria is included in the transaction price. Assess your experience with similar types of performance obligations in making this determination.

Step 4: Allocate the transaction price

Transaction price should be allocated to distinct performance obligations based on relative standalone selling price. This may be the standalone selling price of a good or service when sold separately to a customer in similar circumstances and to similar customers. If a standalone selling price is not directly observable, estimate it by considering all information that is reasonably available, such as market conditions, specific factors, and class of customers.

Step 5: Recognise revenue when the performance obligation is satisfied

Recognise revenue when the promised goods or services are transferred to the customer and the customer obtains control. This may be over time or at a point in time.

The new standard provides indicators when control is transferred. Additionally, the new standard introduces a new concept and revenue is required to be recognised over time when:

i) the asset being created has no alternative use to the company; and
ii) the company has an enforceable right to payment for performance completed to date.

What are some of the most significant changes to the automotive industry?

Allocating transaction prices to the additional goods and services offered

Any additional goods or services offered such as free services and extended warranty programmes that are distinct from the sale of vehicle must be separately recognised, and any discounts or rebates on the contract price are generally allocated to the separate elements.

Identifying performance obligation when additional goods or services are offered

Whether additional incentives offered by distributors are accounted for as a sales incentive or as a performance obligation requires qualitative assessment based on individual facts and circumstances. The offer of additional incentives by distributors is a performance obligation if there was a valid expectation by the dealers that the distributor would offer such incentives, for example if the offer was explicit in the contract or implied by the distributor's past business practices.

Recognition at a point in time, or over time

The point at which revenue is able to be recognised may shift: The change to a control-based standard (as opposed to the guidance under the current standard which is primarily based on the transfer of risks and rewards) will require careful assessment of when an entity should recognise revenue.

Its impact on automotive companies

The table below shows some of the potential impact on the automotive industry arising from the new standard:

Defining the contract (see Illustration 1)

The new standard applies only to contracts with customers. A contract is an agreement between two or more parties that creates enforceable rights and obligations. A contract does not exist if both parties have the unilateral right to terminate a wholly unperformed contract without penalty.

Entities need to determine whether they should account for two or more contracts with the same customer together. Combining contracts, when appropriate, helps to ensure that the unit of accounting is properly identified, and the model is appropriately applied. Contracts should be combined and accounted for as one contract if the contracts are entered into at or near the same time and if one or more of the following criteria are met:

- The contracts are negotiated with a single commercial objective;
- The amount of consideration in one contract depends on the price or performance of the other contract; or
- The goods or services promised are a single performance obligation.

Contract modifications are common in the automotive industry and come in a variety of forms, including changes in the amount of goods to be transferred or previously agreed pricing. Contract modifications might need to be accounted for as a new contract, or combined and accounted for together with the existing contract.

Identifying separate performance obligations (see Illustrations 2 & 3)

The objective of identifying and separating performance obligations is to recognise revenue when the performance obligations are satisfied (that is, when the goods or services are transferred to the customer). Contracts must be evaluated to ensure that all performance obligations are identified. A performance obligation is a promise to transfer a distinct good or service (or a series of distinct goods or services that are substantially the same and have the same pattern of transfer) to a customer. The promise can be explicit, implicit, or implied by an entity's customary business practice.

A good or service is 'distinct' if both the following criteria are met:

- The customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer; and
- The entity's promise to transfer the good or service is separable from other promises in the contract.

A series of distinct goods or services has the same pattern of transfer to the customer if both of the following criteria are met:

- Each distinct good or service in the series that an entity promises to transfer consecutively to the customer would be a performance obligation satisfied over time; and
- A single method would be used to measure the entity's progress toward satisfaction of the performance obligation to transfer each distinct good or service in the series to the customer.

It is common for distributors to offer additional incentives (either cash rebates or free goods or services) after the sale of the vehicle to the dealer to assist with the sale to the end-user. If the distributor includes a good or service in an arrangement with no change to the total price, the additional good or service may need to be accounted for as a separate performance obligation.

Determine and allocate the transaction price (see Illustrations 3 & 4)

The transaction price is the consideration the entity expects to be entitled to in exchange for transferring promised goods or services to a customer. The transaction price is readily determinable in most contracts because the contract promises to pay a fixed amount of cash that is due when the entity transfers the promised goods or services. Certain contracts are however, more complex, such as contracts with stated price increases or decreases over time or with volume pricing adjustments. The transaction price allocated to performance obligations in an arrangement is also affected by consideration payable to the customer (or to the other party that purchases the entity's goods or services from the customer) and time value of money.

Variable elements such as discounts, rebates and incentives given to customers are factored into the transaction price either using the "expected value" or "most likely amount" approach, whichever best predicts the consideration the customer is entitled to. Past experience on take-up rates and external factors will be considered in determining the consideration. There is also a constraint whereby variable consideration is included in the transaction price only to the extent that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur when uncertainty associated with the variable consideration is subsequently resolved. The estimate should be updated at each reporting period.

Amounts paid to a customer (e.g. cash rebate) or to other parties that purchase the entity's goods or services are either a reduction of the transaction price, a payment for distinct goods or services that the entity receives from the customer, or a combination of both. If the consideration paid is a reduction of the transaction price, management shall recognise the reduction at the later when the entity recognises revenue for the transfer of the related goods or services to the customer or when the entity pays or promises to pay the consideration to the customer (even if payment is conditional on a future event).

The transaction price (and any subsequent changes) is allocated to each performance obligation based on relative stand-alone price. The stand-alone selling price should be estimated if the actual selling price is not directly observable. Possible estimation methods include cost plus a reasonable margin, market prices for similar goods or services or the residual approach when the selling price is highly variable. An entity must allocate a discount or variable consideration entirely to one (or more) performance obligations if certain conditions are met.

Recognising revenue (see Illustrations 5 & 6)

Revenue is recognised upon the satisfaction of an entity's performance obligations, which occurs when control of a good or service transfers to the customer. The change to a control-based standard will require careful assessment of when an entity should recognise revenue. An entity should determine at contract inception whether control of a good or service is transferred over time or at a point in time, by assessing whether the performance obligation is satisfied over time. If not, the good or service transfers at a point in time.

An entity recognises revenue over time if any one of the following criteria are met:

- the customer concurrently receives and consumes the benefits provided by the entity's performance as the entity performs;
- the entity's performance creates or enhances a customer-controlled asset; or
- the entity's performance does not create an asset with alternative use and the entity has the right to payment for performance completed to-date.

An entity recognises revenue at a point in time (when control transfers) for performance obligations that do not meet the criteria for recognition of revenue over time. To determine when a customer obtains control and an entity satisfies a performance obligation, the entity should consider the following indicators:

- The seller has the right to payment
- The customer has legal title
- The customer has physical possession
- The customer has significant risks and rewards of ownership; and
- The customer has accepted the asset.

No one indicator is determinative on a stand-alone basis.

Illustration 1:

A supplier enters into two contracts in the same week with an Original Equipment Manufacturer ("OEM") to:

i. construct a tool for the OEM (hereinafter referred to as the "Tool"); and
ii. supply the OEM parts using the Tool

Title of the Tool transfers to the OEM prior to the production of the parts under the supply contract, and the supplier will recover its cost for the Tool through a separate payment from the OEM equal to the supplier's cost of the Tool. Payment for the Tool is due upon completion of the Tool and its approval by the OEM.

Should the supplier combine the contract to produce the parts using the Tool?

Given that the two contracts were entered into near the same time, the supplier will need to combine the two contracts, if:

i. they were negotiated as a single package with a single commercial objective;
ii. the consideration under one contract is dependent on the pricing of the other; or
iii. the goods promised under the two contracts were negotiated with a single commercial objective (constructing the Tool and providing the related parts that will be produced using it) and that pricing is related (no profit margin on the Tool).

In Illustration 1, it appears that the two contracts were negotiated with a single commercial objective (constructing the Tool and providing the related parts that will be produced using it) and that the pricing is related (no profit margin on the Tool). Therefore, the supplier should combine the two contracts based on the facts presented.

Illustration 2:

A distributor sells vehicles to its dealers with a promotion of three years of free maintenance on each vehicle in order to assist its dealers in selling the vehicles to the end customers. The promotion also applies to all of the vehicles that are on the dealer lots (i.e. the vehicles have yet to be sold to the end customers, but have already been sold by the distributor to the dealers) at no additional charge to the dealer. The transaction with the dealer qualifies as a sale because control of the vehicle transfers to the dealer when the vehicle is delivered.

Should the addition of free maintenance be accounted for by the distributor as a sales incentive or as a performance obligation? Is there a different treatment for vehicles currently in the dealer's inventory versus new sales to dealers after the incentive is announced?

In Illustration 2, free maintenance included as part of contracts for new sales to dealers is a performance obligation and therefore a portion of the total transaction price should be allocated to it.

Important!

Whilst the new sales made to the dealers subsequent to the announcement is eligible for the free maintenance promotion, there is a need to consider whether there was a valid expectation by the dealer that the distributor would offer such incentives, with respect to the inventory on the dealer lots. The offer of free maintenance is a performance obligation if it was part of the original contract between the distributor and the dealer, whether the offer was explicit in the contract or implied by the distributor's prior business practices. This is a qualitative assessment based on individual facts and circumstances, and different conclusions can be reached based on different fact patterns. For example, the distributor could conclude that the dealer did not have reasonable expectation for certain items (such as free maintenance) if they are being offered for the first time, on a limited basis, and with no anticipation of repeating the offer.

Illustration 3:

A dealer enters into a sale arrangement with two different customers: Customer A and Customer B. Each customer purchases a vehicle which comes with a 3-year standard warranty and the customer has the option to purchase the dealer's Tender Loving Care ("TLC") package comprising an additional top-up warranty for a 2-year period. The stand-alone selling price of the vehicle with the standard warranty package is RM230,687 and the selling price of the vehicle with the standard warranty and with the TLC package is RM235,687. The standard warranty is not sold separately by the dealer. The stand-alone selling price of the TLC package which can be sold separately is RM6,888.

Would the TLC package be a separate performance obligation of the dealer?

The dealer needs to determine whether sales of the vehicle and TLC package are distinct and therefore should be accounted for as two separate performance obligations.

In Illustration 3, the customer can benefit from the vehicle and the TLC package separately as they are sold separately in the marketplace. Furthermore, there is no integration of the vehicle and the top-up warranty, nor is the vehicle highly inter-related with the top-up warranty. Therefore, the vehicle and the TLC package are distinct performance obligations.

The consideration for the separately purchased TLC package is received at the time the vehicle is delivered to the customer, yet the performance obligations are typically satisfied over the contract period. If a significant financing component exists, the transaction price allocated to the TLC package should reflect the time value of money as interest income under MFRS 15.

How should the transaction price be allocated?

The transaction price is allocated to each performance obligation i.e. the vehicle and the TLC package based on their relative stand-alone selling price.

The table below indicates the effect of applying the guidance under MFRS 15 on a contract with separate performance obligations:

	Customer A (Excluding TLC package)	**Customer B** (Inclusive of TLC package)
	RM	RM
Upon sales of motor vehicle	(a) 230,687	(b) 228,855
1st year	-	-
2nd year	-	-
3rd year	-	-
4th year	-	(c) 3,416
5th year	-	(c) 3,416

(a) The amount of consideration paid by the customer is not allocated to separate performance obligations as the standard warranty is not sold separately. The dealer does not sell the vehicle without the warranty (i.e. not separable), nor does any other dealer of another marque of a similar product.

(b) The amount of consideration paid by the customer is allocated to separate performance obligations based on the proportion as computed below:

Upon sale of motor vehicle = (RM230,687/(RM230,687+RM6,888)) * RM235,687
= RM228,855

(c) Revenue in relation to the TLC package is recognised in the 4th and 5th year on a straight-line basis when the separate performance obligation is performed (i.e. the extended warranty is only effective after the 3-year standard warranty has lapsed, hence revenue is recognised in the 4th and 5th year).

The amount of consideration allocated to the TLC package is based on the proportion as computed below:

Upon satisfaction of performance obligation relating to TLC package
= (RM6,888/(RM230,687+RM6,888)) * RM235,687
= RM6,832 over a 2-year period, or RM3,416 per year

No provision for the costs in relation to the extended warranty should be recognised upfront, and the costs incurred should be recognised as and when the cost of performing its obligations under the extended warranty is incurred. Notwithstanding the foregoing, a dealer should monitor the costs in relation to the performance of obligations under the extended warranty programme, for onerous contract.

Illustration 4:

A distributor sells a vehicle with 3 years maintenance to its dealers for RM190,587. The stand-alone selling price of the vehicle and the maintenance services is RM190,587 and RM1,628 respectively.

However, after the distributor's sale of the vehicle to its dealers but prior to the dealer's sale to the end customers, the distributor adds an additional rebate of RM6,821 which was not contemplated when the vehicle was sold to its dealers.

How should the distributor account for the added incentive of RM6,821 – specifically should it be allocated to both the satisfied and unsatisfied performance obligations or to just the remaining unsatisfied performance obligation?

Rebates are variable considerations and are accounted for as an adjustment to the transaction price. A change in the transaction price that does not involve a contract modification is normally allocated to each performance in the contract on the same basis as at contract inception, which includes satisfied and unsatisfied performance obligations.

The transaction price is therefore reduced by RM6,821 and, using the relative stand-alone selling prices of the two performance obligations, RM6,821 is allocated to the vehicle and free maintenance in the proportionate amounts of RM6,763 (RM6,821 x RM190,587/RM192,215) and RM58 (RM6,821 x RM1,628/RM192,215) respectively.

The amount allocated to a satisfied performance obligation (in Illustration 4, the vehicle) is recognised as a reduction of revenue in the period where the change in transaction price occurs.

Illustration 5:

A supplier enters into a contract with an Original Equipment Manufacturer ("OEM") to:

i. construct a tool for the OEM (hereinafter referred to as the "Tool"); and
ii. supply the OEM parts using the Tool

The Tool and the supply arrangements are separate performance obligations and the supplier would incur significant economic losses if it were to attempt to re-work the Tool for another OEM if the OEM terminates the contract (that is, there is no alternative use for the Tool). The OEM is contractually obligated to reimburse the supplier for its costs to date including a reasonable profit margin to construct the Tool if the OEM cancels the contract other than for breach.

How should revenue related to the Tool be recognised?

In Illustration 5, the Tool performance obligation is satisfied over time because the supplier's performance does not create an asset with an alternative use and the supplier has the enforceable right to payment which should include a recovery of the costs incurred by the supplier plus a reasonable profit margin.

In other arrangements, the enforceable right to payment may only include recovery of the costs incurred by the entity and therefore an entity may not meet this criterion. In that case, an entity would need to evaluate whether the entity's performance creates or enhances an asset and if the customer controls the asset as it is created to determine if the performance obligation is satisfied over time.

The supplier will need to select the most appropriate method (either an input or output method) to measure its performance over the contract term if revenue is recognised over time. An output method, such as units produced, may be appropriate if the entity includes in its revenue measure the work-in-progress and completed-but-not-delivered items that are controlled by the customer. The supplier might conclude that an input method is more appropriate if there is a direct relationship between the entity's inputs and the transfer of control of goods or services to the customer.

Illustration 6:

Continuing from Illustration 5, assume all the facts in the previous Illustration remains the same, with the exception of the following facts:

i. The OEM can cancel the contract at any time without termination or make-whole payment because the Tool can be readily used to produce parts for other OEMs; and
ii. Title (assumption of control) of the Tool passes to the OEM only upon its completion and acceptance by the OEM.

How should the supplier recognise revenue?

In Illustration 6, the Tool has an alternative use to the supplier, and control of the Tool is not transferred to the OEM during the work-in-process phase. The supplier also does not have the right to payment for performance completed to date (including a reasonable profit margin) in the event of a contract termination by the OEM. Revenue should be recognised when the Tool is completed and control of the Tool is transferred to the OEM.

What can go wrong?

While the effective date may seem a long way off, it is important to understand the implications of applying the standard. Key impact will be to revenue profile, to certain cost recognition and ultimately profit recognition. An assessment will be required that will reinforce the notion that planning for implementation should start early.

Here are some of the anticipated common issues when applying the new standard for the first time.

Lack of judgement used in meeting requirements of the new standard

In the automotive industry, product warranties given to the customers by the OEMs and suppliers are found to be relatively common.

The new standard draws a distinction between product warranties that the customer has the option to purchase separately and those that cannot be purchased separately. These entities will need to exercise judgement when assessing warranties which are not sold separately to determine if there is a service component inherent in the warranty that needs to be accounted for as a separate performance obligation.

The lack of the exercise of judgement in assessing as to whether there is a single or multiple performance obligation in this area will consequently result in the incorrect timing of revenue recognition.

Determination of control

The new standard implies that revenue is recognised upon the satisfaction of an entity's performance obligations, which occurs when control of a good or service transfers to the customer, instead of the transfer of risks and rewards under the current guidance. Control can transfer either at a point in time or over time. The change to a control-based standard will require careful assessment of when an entity should recognise revenue.

The timing of when revenue is recognised might be consistent with the current practice for many automotive contracts related to the sale of production goods, but may however need to be separately accessed for tooling contracts, engineering, research and development contracts.

It is crucial for these automotive entities to ensure that proper assessment is being made in accessing the terms of the contract to determine if the control transfers at a point in time or over time.

Mismatch of cash flows and revenues

Revenue recognition is largely dependent on determination and allocation of transaction price and the terms explicit or implied in contracts with customers. Such identification and allocation must be carefully scrutinised in line with the requirements of the standard during the contract negotiation stage to avoid surprises. Other key capital items, if any, would need to be deliberated hand in hand with revenue and cash flow planning.

Conventional Key Performance Indicators ("KPIs") for revenue are no longer comparable historically

As a result of different product offerings, and increased involvement of significant judgement on estimated stand alone selling prices, conventional revenue KPIs such Average Gross Profit Margin and EBITDA et. al. may no longer be comparable with prior periods, or even with other competitors.

Tax and Regulatory Implications

With the widening gap between timing of revenue recognition and cash received, as well as changes in timing of expenses and capitalised costs, this may significantly impact current tax planning that companies have in place.

Inadequate management processes

Management process flow must be in place in order to identify, assess and conclude on the treatment before key products are introduced to the market. The formalisation of a dynamic management process must be in place to enable timely assessment and reaction to competition in the market. This includes preparation and maintenance of supporting documentation to document judgement and estimates. Without a dynamic and complete management process in place, data for assessments may be outdated or incomplete, automotive companies could be laggards behind competition and even risk erroneous conclusions, resulting in deviations from budgets or even financial losses. Design and implementation of management processes will require technical expertise.

Lack of documentation on judgements and estimates

Revenue recognition policies for individual products largely depends on management's judgement and estimates subsequent to careful assessment. Documentation on the basis of judgement and estimates based on facts must be in place to withstand scrutiny by auditors, tax authorities and regulators. Close collaboration between Legal, Sales and Marketing, IT, Business Development and Finance teams are essential in arriving at decisions from planning up to launching of products. Lack of documentation could result in inconsistency of application and the lack of an audit trail in the event of review, leading to potential restatement of financial results.

Other matters to consider

Contracts may need to be revisited

Existing terms could take on new meaning under the new standard, so you may need to re-negotiate debt covenants or earn-out arrangements to maintain the original intent. You may also want to rethink how you structure customer agreements in the future, for example if you want to achieve recognition over time rather than at a point in time.

Compensation and bonus plans may need to be analysed

Revenue recognition can trigger payments like bonuses or commission. You will need to consider how timing changes for revenue recognition may affect these and other internal arrangements.

Financial disclosures may need to be enhanced

Companies also need to be more transparent and deeper in disclosing revenue recognition policy and arrangements.

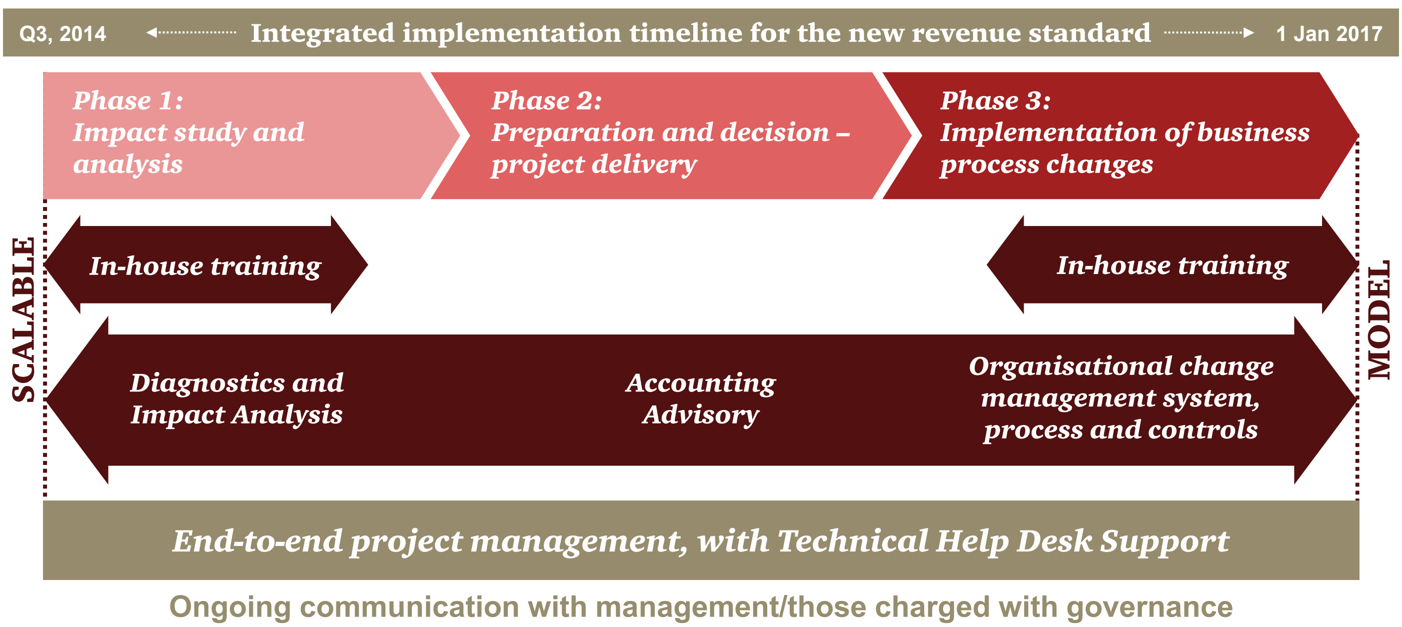
Investor relations plans need to be developed

Stakeholders may want to understand how revenue recognition will change and how the new standard affects your company's financial picture.

How we can help

Our 'one firm' solution

PwC is already working with a number of large companies around the world to manage their transition to the new standard. We have developed an approach that draws on our expertise in accounting, systems implementation and transaction structuring to deliver an end-to-end integrated solution.



Described below are some of the ways in which we can help you as you plan for adoption. All the services described below can be customised to suit your needs.

Service	What we will do
In-house training and technical help-desk	• Provide you with training for your accounting, IT, legal and compliance teams on specific areas and implementation issues you may face • Provide on-going implementation and technical support to finance team and other cross-functional teams on ad-hoc questions through transition phase
Diagnostics	• Perform diagnostic review of your existing arrangements / accounting policies to assess business issues and financial reporting implications and provide proposed practical solutions and recommendations • Perform diagnostic that includes understanding the financial and cross-functional impact; analyse your business models and contracts underlying your revenue recognition; analyse your IT landscape and an overview of risks and gaps. This will help you understand the breadth and depth of the impact (e.g. accounting, reporting, sales contracts, controls and process, systems, remuneration, taxes and investor relations) so you can plan for implementation
Impact analysis	• Work closely with your finance team to model the impact of adoption under different revenue recognition scenarios to your earnings, business model, compensation plans, debt covenants and any other impact areas identified by you • Perform a detailed analysis of differences in accounting policies, data gaps and IT systems landscape including required interfaces to be deployed / upgraded based on business requirement and functional design specifications • Based on the impact analysis, develop and execute a cross-functional communication strategy both internally and externally to your investors, audit committee, board of directors and other stakeholders on a timely basis
Accounting advisory	• Undertake a detailed analysis of your specific revenue contract considering your business model while also being mindful of your objectives and propose possible solutions for you • Active participation on the implementation of the proposed solutions, for example, participation in discussions with your lawyers for possible changes to contracts, internal meetings with other cross-functional teams to coordinate implementation, etc
Systems, process and control	• Work with your finance and IT teams on updating revenue recognition process, system change, books and records through the transition period • Collaborate with your finance and IT teams on updating revenue recognition process, contract reviews, system change, books and records through the transition period • Support you to determine a sustainable software solution that is able to support compliance with the complex accounting requirements for revenue recognition
Full Scale Implementation	• A combination of all of the above to assist with your full scale implementation of the standard (from implementation in-house education, initial diagnostic phase, impact analysis, to embedding changes in your financial reporting tool) utilising PwC developed and tested implementation tools and methodologies • Support you in gathering the data, testing IT concept, adjusting IT systems and testing the results

Appendix: Implementation plan

Here is an example of some of the key areas and activities you may wish to consider in your implementation plan:

Key stages	Overall objectives	Key activities	Done?
1. Inception and Baseline	Determine and quantify existing business transactions that carry an implication to the MFRS 15	• Understand existing retail and enterprise packages and contractual arrangements • Understand existing dealer incentive plans and bonuses • Identify separate performance obligations and incremental costs through the contracts and plans review • Compile volume of transactions under each package and plan	
2. Information Gaps and Impact Study	Identify information gaps for MFRS 15 compliance and to conduct a business and financial impact study	Assess Information Gaps • Agree approach to determine transaction price • Identify information required to meet MFRS 15 requirements • Assess the availability of information through existing system or manual sources • Explore options to address the information gaps (e.g. IT enhancement or package re-structuring) Conduct Impact Study • Conduct high level financial impact study to simulate the financial impact of MFRS 15 on Company performance • Conduct a business impact study based on the options available, taking into consideration existing process and IT infrastructure • Develop decision paper for adopting “Contract” or “Portfolio” approach. The decision paper shall contain a cost benefit analysis and project risk assessment (e.g. project complexity and ability to deliver on time)	

Here is an example of some of the key areas and activities you may wish to consider in your implementation plan: (cont'd)

Key stages	Overall objectives	Key activities	Done?
3. Solution Design	Design the detailed solutions and implementation roadmap	• Work with respective business divisions to develop a solution blueprint that clearly defines: − the IT enhancements initiatives; − Refinement of incentive plans; − Fine tuning of existing contract templates and processes; − Revision of bundling packages, if applicable • Develop implementation plans and roadmap • Seek endorsement and commitments from all business partners	
4. Solutions rollout	Develop all changes required on the systems, policies, processes and templates. Train the relevant stakeholders and roll out to the operations	• Construct IT enhancements and develop tracking database • Complete system testing and user training • Update Policies & Procedures to incorporate new processes and controls to capture information to meet MFRS 15 requirements • Update relevant templates and forms jointly with the business owners (e.g. contract template, incentive calculation, tax computation, budget and management report, etc.) • Develop guideline and processes for the development of new Incentive Plans and bundling packages in the future • Streamline and refine existing incentive plans and bundling packages, if applicable • Conduct rollout training and final rollout to the operations	
5. Revenue reporting and post implementation optimisation	Assess impact of new revenue reporting and optimise the approach	• Determine transaction prices • Determine standalone transaction prices • Allocate the transaction price to separate performance obligations • Simulate financial closing with MFRS 15 requirements to assess the financial impact to company performance • Update company budget or targets	

Let's talk

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