MALAYSIAN INSTITUTE OF ACCOUNTANTS
FINANCIAL REPORTING STANDARDS IMPLEMENTATION COMMITTEE
("FRSIC")

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Treatment of Land Cost in the Input Method

The issue:

Paragraph 39 of IFRS 15, Revenue from Contracts with Customers states that "For each performance obligation satisfied over time in accordance with paragraphs 35-37, an entity shall recognise revenue over time by measuring the progress towards complete satisfaction of that performance obligation." Paragraph 41 of IFRS 15 states that "Appropriate methods of measuring progress include output methods and input methods."

The objective of this accounting paper is to explore how should land cost be treated when an input method is used to measure an entity's progress towards complete satisfaction of a performance obligation, specifically by a property developer when revenue is recognised over time.

This accounting paper also makes the following assumptions:
1) Land is not a separate performance obligation, e.g. in a multi-unit development such as apartment or condominium.
2) The criteria to recognise revenue over time are met.

Current accounting practice as observed by the Submitter:

At present, paragraph 37 of FRS 201, Property Development Activities states "When the stage of completion is determined by reference to the property development costs incurred to date, only those property development costs that reflect work performed are included in costs incurred to date. Examples of costs that do not relate to work performed are cost of land, financing costs capitalised to the project, and payments made to contractors in advance of work performed under the project.

Reasons for the FRSIC to address the issue:

Paragraph 42 of IFRS 15 states "When applying a method for measuring progress, an entity shall exclude from the measure of progress any goods or services for which the entity does not transfer control to a customer. Conversely, an entity shall include in the measure of progress any goods or services for which the entity does transfer control to a customer when satisfying that performance obligation." Whilst IFRS 15 does not define control, paragraph 33 of the standard explains that "Control of an asset refers to the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset."

It is possible that there will be divergence in views whether the buyer has obtained control over

Dewan Akauntan, 2 Jalan Tun Sambanthan 3 Brickfields, 50470 Kuala Lumpur, Malaysia
[Web] http://www.mia.org.my [Phone] + 60 3 2279 9200 [Fax] + 60 3 2274 1783

land, when IFRS 15 is adopted by the property development industry in Malaysia.

If buyer has obtained control over land, then applying IFRS 15.42 would mean that land cost should be included in the input method when measuring progress in an input method.

If buyer has not obtained control over land, then applying IFRS 15.42 would mean that land cost should be excluded in the input method when measuring progress in an input method.

Submitter's proposal or recommendation to address the issue:

Paragraph 33 of IFRS 15 also provides the following guidance in regards to "control" where it states "Control includes the ability to prevent other entities from directing the use of, and obtaining the benefits from, an asset. The benefits of an asset are the potential cash flows (inflows or savings in outflows) that can be obtained directly or indirectly in many ways, such as by:

(a) using the asset to produce goods or provide services (including public services);
(b) using the asset to enhance the value of other assets;
(c) using the asset to settle liabilities or reduce expenses;
(d) selling or exchanging the asset;
(e) pledging the asset to secure a loan; and
(f) holding the asset.

Following the guidance from IFRS 15.33 would suggest that the buyer has obtained control over land since:

- buyer could sell to another party its right under the Sales and Purchase Agreement ("SPA"), hence effectively sells the underlying land and construction work-in-progress (i.e. example (d) above).
- buyer could pledge the land to secure bank borrowing (i.e. example (e) above). This happens in reality in Malaysia where majority of property buyers are loan buyers.

Further, by entering into the SPA, buyer is also able to prevent the developer from using the land for any other purpose other than for the development of the intended property purchased by buyer.

Based on the above assessment, land cost should be included in the input method when measuring progress in an input method.

Submitted on:

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Corresponding Guidance:

Malaysian Institute of Accountants
Dewan Akauntan, 2 Jalan Tun Sambanthan 3 Brickfields, 50470 Kuala Lumpur, Malaysia
[Web] http://www.mia.org.my [Phone] + 60 3 2279 9200 [Fax] + 60 3 2274 1783