

**PRACTICAL APPLICATION OF IFRS THE WAY TO MAKING EFFECTIVE
FINANCIAL, MANAGERIAL AND ECONOMIC DECISIONS**

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Abstract: This article lists the problems of IFRS implementation, interprets the key points of IFRS 15 “Revenue from Contracts with Customers” and examines issues of its practical application. The core principle of the standard is that an entity should recognise revenue from the transfer of promised goods or services to customers at an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. In order to make it better understandable for the reader, examples are given on the disclosure of the essence of revenue accounting with a reflection of their impact on the company's financial statements in the form of an excerpt from the statement of financial position and the profit and loss statement.

Key words: revenue, financial condition, contract, transaction price, buyer, obligations to perform, cost price, methods of determination, net profit.

Introduction. The implementation of International Financial Reporting Standards is necessary to increase the transparency and comparability of financial statements of economic entities and the public sector, which allows for more informed management and economic decisions.

IFRS provide a unified approach to reporting, making information more understandable and comparable for internal and external users. More reliable and complete financial information enables effective financial, management and economic decisions. A single international standard facilitates interaction with international financial organizations and obtaining external financing.

There is currently a gradual increase in the number of joint-stock companies, commercial banks, insurance companies, large taxpayers and even the private sector applying IFRS. This is caused by the increase in the number of large contracts concluded with Western partners, with the attraction of funds from foreign investors, and with the increase in the volume of borrowed funds received from foreign financial institutions.

But despite this, it should be noted that there are some problems in the practical issues of applying IFRS in Uzbekistan. These are:

1. Lack of experience and education in the field of international standards. Training accountants, auditors and financial specialists so that they can understand and correctly apply IFRS requires time and resources.

2. There is no algorithm for transformation from NAS to IFRS.

3. The problem of training specialists in IFRS is especially acute. In order for the trained person to become a real specialist who can qualitatively solve production issues, practical work experience is needed. But it is not there. And there are also few places where it can be purchased in the republic, because all enterprises are at the stage of introducing and implementing IFRS

4. The fundamental difference between IFRS and NAS is that professional judgment plays a significant role in IFRS. This is precisely what we do not have yet, because these skills are acquired over the years.

5. IFRS are complex and require in-depth accounting knowledge, which can be difficult for professionals. There is often a shortage of professionals with the necessary training and experience to apply these standards in businesses, in the public and private sectors.

In order to find a solution to the listed problems, in this article we want to explain the essence of IFRS 15 “Revenue from customers” and give some explanations of the organization of revenue accounting according to international standards and the preparation of financial statements, showing their practical application using specific examples.

When assessing the financial condition of an organization, revenue, along with net profit, is the most important item in financial statements. However, net profit cannot be determined without an estimate of revenue, which is typically the most significant item in the statement of comprehensive income. IFRS 15 introduces a new revenue recognition model and significantly increases the scope of disclosure requirements. The standard will certainly affect and in many cases significantly change companies' approaches to revenue recognition.

The purpose of this article is to consider individual theoretical provisions of the standard and analyze how they will affect the company's existing approaches to revenue recognition.

• IFRS 15 introduces a fundamentally new concept for revenue recognition. It introduces a number of new concepts and new guidance on certain revenue recognition issues, such as:

- separate obligations to perform a contract;
- new guidance on when revenue is recognized;
- the concept of variable consideration, which is used to determine the amount of revenue recognized when the amount of revenue may vary;
- new guidance on the allocation of the transaction price among individual obligations;
- accounting for the time value of money.

Methodology. When conducting research work on this topic, the conceptual foundations of international financial reporting standards, regulatory frameworks for accounting in Uzbekistan and abroad were studied, The scientific works of foreign and domestic economists on accounting for revenue recognition based on IFRS using methods of data collection, generalization, grouping, comparison, induction and deduction, comparison and reflection in financial statements were used.

Results. The criteria for revenue recognition under IFRS 15 are:

- The result of ordinary activities;
- The gross receipt of economic benefits of the company for the current period;
- Leads to an increase in equity other than contributions from owners.

The source of revenue depends on the company's main activity. In particular, the organization may be engaged in the production of finished products. However, companies may engage in other activities, such as providing works and services, lending money and earning interest income, can lease out licensed services and receive license payments (royalties), some operate on contributions to the authorized capital of other enterprises and receive dividends, and this will be the company's revenue.

In terms of IFRS 15 Revenue from Contracts with Customers, examples of revenue are:

- Revenue from the sale of finished products and goods
- Revenue from the provision of works and services
- Interest income
- Royalty payments
- Dividend income

What needs to be done to recognize revenue or income from core activities in financial statements? With the introduction of Standard 15, the revenue recognition process has become strictly regulated, and a company must perform 5 steps in sequence before reflecting income in the profit and loss statement. The next step checks the revenue recognition criteria.

5 steps to revenue recognition:

1. Identify the existence of a contract with a customer.

2. Identify the obligations to be performed under the contract.
3. Determine the transaction price.
4. Allocate the transaction price to all obligations to be performed.
5. Recognize revenue.

Analysis. And so, step 1, which the company takes to recognize revenue.

In order to identify the existence of a contract with the buyer, first you need to determine who the buyer is.

IFRS 15 gives us the following definition:

A customer is a party that has entered into a contract with an organization to receive goods or services that result from the organization's ordinary activities in exchange for consideration.

So when do we have a contract with a customer?

Standard 15 lists 4 criteria for recognizing a contract.

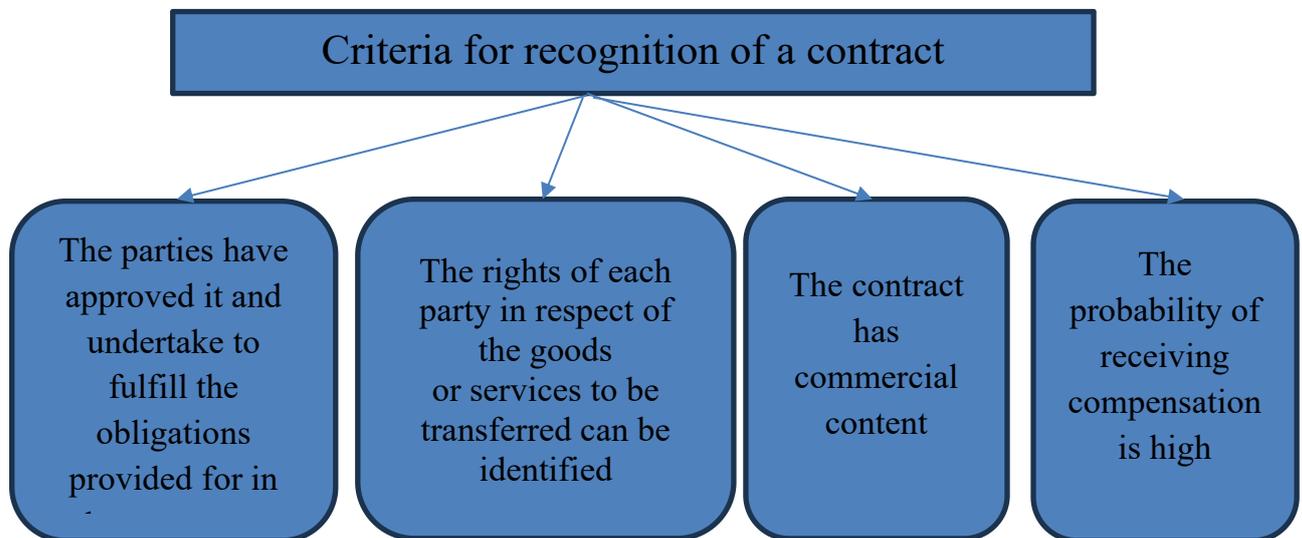


Figure 1. Criteria for recognition of a contract

After recognizing all these 4 criteria, we can say that the Treaty exists. Let's look at an example.

Example 1. The company sells vacuum cleaners. In order to expand the product range, the company's management decided to exchange red vacuum cleaners for similar blue vacuum cleaners.

- No commercial content of the transaction.
- Revenue is not recognized.

Example 2. The company entered into a contract with a buyer, which, as it turned out, was subject to forced bankruptcy proceedings.

- The probability of payment under this contract is low.
- The company does not recognize revenue from the sale.

IFRS specifies the conditions under which the contract does not exist, which means the company does not recognize revenue.

Each party has a legally enforceable right to unilaterally terminate a contract that has not been fulfilled in any part. In this case, the contract does not exist. What does this mean? Let's look at a real example.

The company has entered into a contract for the provision of consulting services. Let us assume that, according to the current legislation, the buyer company has the right to terminate

the contract within 30 days without compensating the counterparty for the costs incurred during this period.

- There is no likelihood of receiving economic benefits.
- The contract does not exist.

At the same time, the company does not have the right to reflect revenue in the profit and loss statement for the first 30 days.

What to do if in this contract the supplier received some amount of advance payment? The amount of advance payment received by the supplier is reimbursed. Any compensation received by the supplier in a situation where the contract does not exist is equal to liabilities (accounts payable).

Example. A company entered into a letter of intent with a real estate buyer. The buyer made an advance payment of 1 million USD.

- Since the buyer has the right to terminate the transaction, the contract does not exist.
- The funds received are the company's debt to the buyer.

This is reflected in the statement of financial position as follows:

Table 1

Impact of the transaction on the statement of financial position (extract), USD million

Assets	Sum	Capital and liabilities	Sum
Cash	1,0	Accounts payable to buyer	1,0

The second step in revenue recognition from the point of view of IFRS No. 15 is to determine the amount of the obligation to be performed by the seller under the contract in favor of the buyer. What are contractual obligations and how to distinguish them from each other, these are the questions we will consider now. First, let's look at the definition of contractual obligation from IFRS 15.

The obligations to be performed under a contract are the distinct goods or services that the seller has promised to provide to the buyer under the contract. Within this definition, the key word here is distinct goods, i.e. one good or service can be separated from another good or service. The question arises how this separation occurs? The standard tells us what distinct goods mean.

Distinguishing goods and services from each other (criteria) are:

1) The buyer can benefit from using either the goods (services) themselves or in combination with other resources available to him.

Example. As a seller, I transfer two objects to my buyer - shampoo and shower gel separately. It is clear that the buyer can use shampoo and shower gel separately, and therefore for him these are distinguishable goods. As a seller, I transfer two objects to the buyer.

2) An entity's promise to transfer a good or service to a customer is separately identifiable from other promises in the contract.

Example. I am a kitchen seller. As a seller, I provided the buyer with a separate service for assembling kitchens. But the buyer can refuse this service. I separately identified in the contract that if the buyer agreed to this service, I will transfer to him the product in the form of a kitchen separately and the service for assembling this kitchen separately.

Let's look at a few more examples that will help us understand what distinct goods, works and services mean.

Example: A company supplies equipment to a buyer and also provides services for installing this equipment.

The buyer has the right to refuse installation of this equipment. The right to refuse is clearly stated in the terms of the contract. How much responsibility do we transfer to the buyer under this contract?

There are 2 obligations under the contract that must be fulfilled:

- Sale and transfer of equipment.
- Provision of services for installation of equipment.

By the way, looking ahead, if we have two distinct services or one product one service, in any case two obligations to be performed under the contract, the company will recognize two or more revenues in the profit and loss statement.

Example. The company sells software, installs it and provides maintenance services for 3 years. Let's determine how many distinct obligations must be performed under this agreement after signing the agreement.

There are 3 obligations under the contract that must be fulfilled:

- 1). Sale of software (the buyer can use this software regardless of other conditions stipulated in the contract)
- 2). Installation of software (the company must recognize revenue separately from this type of service).
- 3). Software maintenance. Moreover, this is a long-term obligation, according to the concluded terms of the contract, this maintenance will be carried out for as long as 3 years, and the company will recognize revenue not at one time, but over these 3 years.

The third step in revenue recognition from the point of view of IFRS 15 is the transaction price, that is, the amount that we are ready to receive from our buyer. Let's see what international standards tell us. First, let's figure out how to determine the transaction price.

The transaction price is the amount of consideration that the organization expects to receive from the buyer. The price should include only the amount that is unlikely to have to be reversed (returned). The components of the transaction price are as follows:

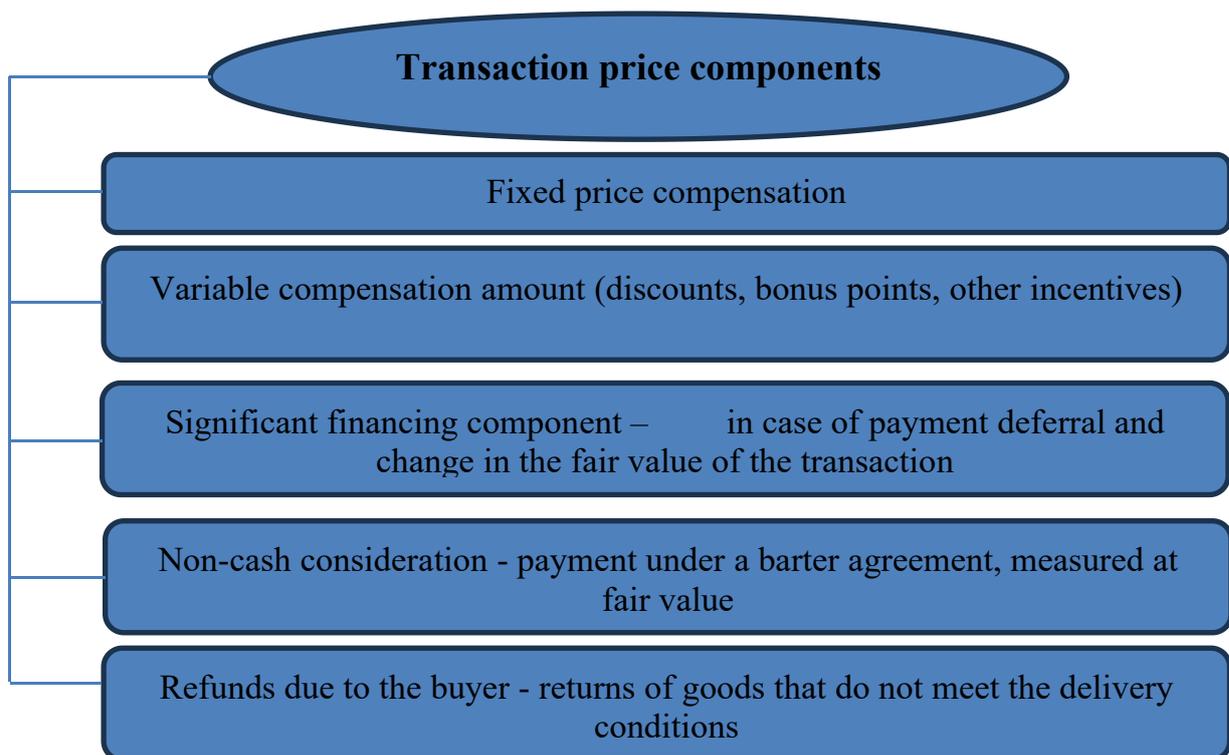


Figure 2. Transaction price components

Example 1. The company entered into a contract for the sale of goods on terms of deferred payment for 1 year. The price of the goods under the contract is 100 thousand USD. The fair value of the goods is 90 thousand USD, the cost of the goods is 50 thousand USD.

The contract has a significant financing component in the amount of 10 thousand USD. Revenue under the contract = 90 thousand USD. This is reflected in the income statement as follows:

Table 2

Impact of the transaction on the profit and loss statement (extract for the year), thousand USD

Revenue	90
Cost of sales	(50)
Profit (loss) from sales	40
Interest income	10
Profit (loss) for the period	50

Example 2. A company has entered into a contract for the sale of goods, the price of the goods under the contract is 1 million USD. According to the terms of the contract, if the buyer buys more goods within 3 months for at least 1 million USD, the company will provide him with a 10% discount.

The cost price of the goods is 0.5 million USD. Revenue is reduced by the amount of the potential discount, i.e. by 0.1 million USD, and this is reflected in the profit and loss statement as follows:

Table 3

Impact of the transaction on the profit and loss statement (extract for the year), thousand USD

Revenue	0,9
Cost of sales	(0,5)
Profit (loss) from sales	0,4

This amount is reflected as a liability in the statement of financial position.

Table 4

Impact of the transaction on the statement of financial position (extract), USD million

Assets	CyMM	Capital and liabilities	Cymma
	a		
Cash	1	Retained earnings (deficit)	0,4
Stocks	(0,5)	Discount liabilities	0,1

And so, in order to determine the price under the contract, you need to look at the presence of all the components that are included in this price. If you have a classic contract in which you clearly fix the amount to be reimbursed from buyers, this is the simplest option for forming a price through a fixed amount of reimbursement. However, life is a more complicated thing, so we will not forget to reduce this price by the amount of potential discounts provided, including the amount of interest that we include in the cost of the contract with a deferment, and by those returns that we potentially expect from the point of view of this contract. After we have calculated the total price under the contract, we must distribute this price between the obligations that we transfer to the buyer.

Thus, in order to recognize revenue, according to IFRS, the company must complete 5 consecutive steps. We have already considered 3 steps out of 5. And now I will suggest you to consider step 4, which is called calculating the cost of obligations subject to execution under the contract. What is the point of this step? Imagine that under the contract you transferred to the buyer not 1 asset, but 2. In total, you received a certain amount. The question arises: How is this amount distributed between 2 goods transferred to the buyer? We must recognize 2 separate revenues from the point of view of IFRS.

So, standard 15 gives us 2 ways to determine the selling price of identified obligations. The company has the right to choose any of the listed methods that it considers more reliable or necessary in a given situation. Let's look at these methods. Methods for determining the selling price of identified obligations:

1. Observed price (business practice). The company knows how much it could sell each item for separately, this is its practice, the practice of its business, and based on this cost it distributes the total price under the contract.

2. Estimated price:

- The "Adjusted Market Price" approach. We can take the market value of this product. That is, see how much it costs from counterparties, from our competitors. Based on this market value, distribute the price of our contract.

- The "**Expected Costs Plus Margin**" approach. What are costs? These are the costs that we can incur to produce our products. Margin, from an IFRS perspective, is the markup or amount of profit that the company expects to receive when selling products under a contract.

- **Residual principle.** In this situation, the company knows exactly the market value of one product that it transfers to the buyer, and determines the price of the remaining products, so to speak, by the residual principle, by subtracting from the total transaction price the reliable estimate that falls on the first product.

Let's look at some examples.

Example 1. A company sells equipment and its installation for 120 thousand USD. We immediately determine how many responsibilities the company transfers to its buyer. We see from this sentence that the company transfers:

- 1). Goods - equipment and
- 2). Installation, that is, services.

To distribute these 120 thousand USD into two parts, we need additional information. In particular, the company tells us:

The price of separate sale of equipment is 100 thousand USD.

Cost of services for installation of equipment is 40 thousand USD.

That is, in fact, if the company sold the equipment and services separately, it would receive 140 thousand USD. Since this buyer takes the goods and services at the same time, the company provided the buyer with discounts, reducing the transaction price to 120 thousand USD.

Let's distribute these 120 thousand USD using the observed prices method.

In order to apply the method of observed prices we must initially anticipate the share of the cost of the equipment in the total price of the contract. But also, as a consequence the share of services for the installation of this equipment.

$100 \text{ thousand USD} / 140 \text{ thousand USD} = 0.71$ Share of equipment in the contract

$0.71 \times 120 \text{ thousand USD} = 85.2 \text{ thousand USD}$. Revenue from sale of equipment

$120 \text{ thousand USD} - 85.2 \text{ thousand USD} = 34.8 \text{ thousand USD}$. Revenue from installation services

Example 2. The company sells land together with a garden for 150 thousand USD. The fair value of the land is 130 million USD. The fair value of the garden is unknown. We use the calculation method, the residual principle.

130 million USD. Proceeds from sale of land

150 million USD - 130 million USD = 20 million USD. Proceeds from sale of garden.

Example 3. The company sells equipment and its installation for 120 thousand USD. Experts estimate that the installation costs are 2 thousand USD. The markup for this type of service is 50%.

We use the calculation method, the “expected costs plus margin” approach.

2 thousand USD x 1.5 = 3 thousand USD. Revenue from installation services

120 thousand USD - 3 thousand USD = 117 thousand USD. Revenue from equipment sales

To summarize step 4, if a company is contractually transferring several responsibilities and expects to receive compensation in a total amount from customers, this price, the total amount, must be divided between all responsibilities and the standards allow us to use several approaches to this process. It is clear that the company must demonstrate the reliability of the assessment of all indicators. And what method we have chosen is our right, which must be recorded in the company's accounting policy. And so we have considered with you the 4th step in recognizing revenue. The last 5th step remains, within which we need to discuss the moments of revenue recognition.

The last step in recognizing revenue in financial statements from the IFRS point of view is its recognition. And here the key question that needs to be answered is the question of the moment of revenue recognition. Now we have the right to recognize it, after some time or over a long period of time. So, from the point of view of Standard 15, the concept of transfer of control is the basis for determining the moment of revenue recognition, and the standard gives us 2 options for calculating this moment.

Revenue can be recognized:

1. At a certain point in time (i.e. on a certain date).

2. Over a certain period of time (depending on the degree of readiness). The second is used if we provide services or perform some work. In order to determine revenue, the company will have to assess the degree of readiness of this work.

Point-in-time revenue recognition. When does point-in-time begin? When the entity meets the 5 recognition criteria.

- The entity has a present right to pay for the asset.

- The customer has title to the asset.

- The entity has transferred physical possession.

- The buyer is exposed to significant risks and rewards associated with ownership of the asset.

- The buyer has accepted the asset.

Let's look at how these criteria are implemented in real examples.

Example 1. The company transferred goods to a retail store, whose income depends on the volume of sales. The retail store does not have the right to set the price of the goods or provide discounts to the buyer. If the goods are not sold within the established time, the goods are returned to the company.

Revenue is not recognized until the goods are sold to the final consumer.

Example 2. The company transferred the goods to a retail store. The goods can be returned only if they do not meet the delivery conditions.

Revenue is recognized over a certain period of time – at the time the goods are transferred to the retail store. Recognition of revenue over a certain period of time means:

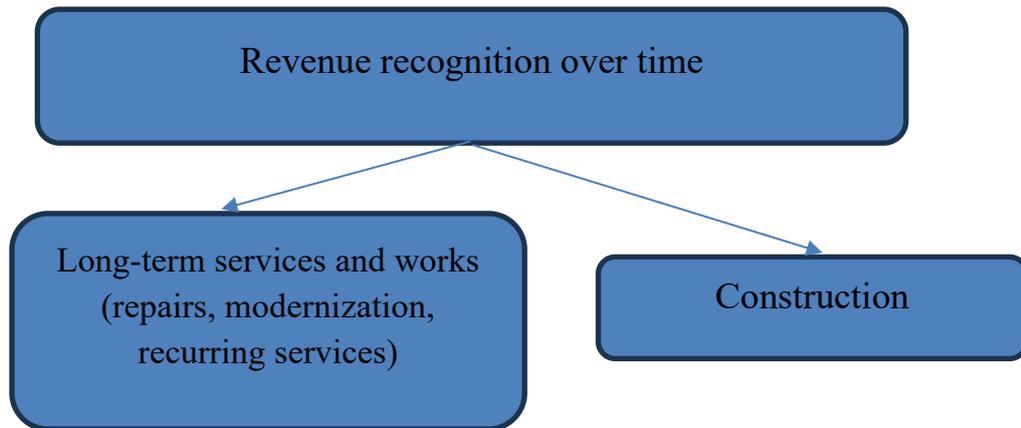


Figure 3. Revenue recognition over time

Example. A company provides financial reporting services. Revenue under this contract will be recognized over the term of the contract. The question arises. How to distribute revenue over this long period of time? In order to do this, we need to assess the degree of work completion. IFRS offers two methods for assessing the degree of work completion. The company must choose one of the methods and reflect it in the accounting policy and adhere to when reflecting revenue. These are:

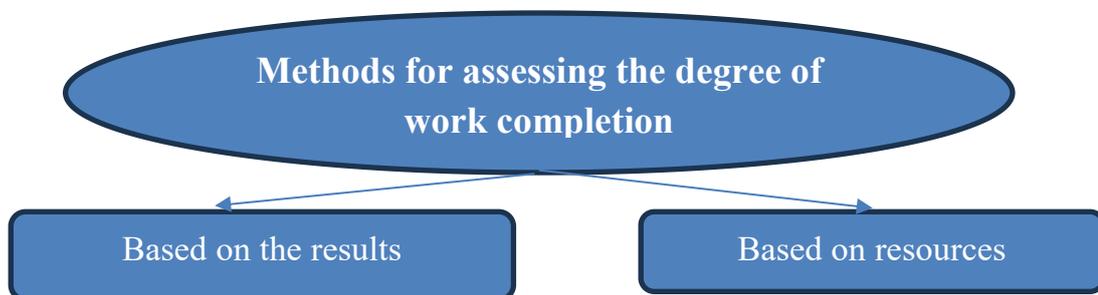


Figure 4. Methods for assessing the degree of work completion

Let's look at examples of using methods for assessing the degree of work completion.

Example. A company is constructing a building commissioned by another organization. The contract price is 100 million USD. The estimated cost of the work is 80 million USD, of which 35 million USD have been incurred to date. According to experts, the building is 50% complete.

Let's apply the "Results-Based" method.

$50\% \times 100 \text{ million USD} = 50 \text{ million USD}$ Current Period Revenue

$50\% \times 80 \text{ million USD} = 40 \text{ million USD}$ Cost of Sales

And if we apply the "Resource-Based" method.

$(35 \text{ million USD} / 80 \text{ million USD}) \times 100\% = 43.75\%$. Share of incurred costs

$(43.75\% \times 100 \text{ million USD}) / 100\% = 43.75 \text{ million USD}$. Current period revenue

$(43.75\% \times 80 \text{ million USD}) / 100\% = 35 \text{ million USD}$. Cost of sales

So, revenue is recognized after the company has defined and gone through all the steps of recognition. And in the last step, we need to understand when this revenue is recognized. And the standards allow us to either recognize it in a certain period of time, or recognize it over a long period of time. In the second case, it is necessary to choose a method for assessing the degree of readiness of the work and, based on this percentage, reflect revenue and cost of sales in the reporting.

At this point, we have considered all the steps of revenue recognition and there is little left to do. We need to understand in which financial reporting indicators all the steps we have talked about will be reflected.

The last question we suggest you consider is the issue of reflecting all revenue recognition transactions in financial statements. Let's see how the sale of goods and provision of services affects certain lines in the financial position statement and in the profit and loss statement. So, from the point of view of IFRS, revenue generation operations will affect 2 reporting forms. The first basic form, where revenue will be reflected, is the Profit or Loss Statement. Why? Because revenue is income from the main type of activity. And we know that income and expenses are reflected in the Profit or Loss Statement. Moreover, transactions related to the sale of goods, provision of services and work are also reflected in the financial position report.

Let's take it in order, let's start with the profit and loss report. We have already considered in previous questions that the profit and loss report reflects two indicators for the contract for the sale of goods or provision of services. First, we will have income from core activities, that is, the first line of the profit and loss report. Do not forget before reflecting revenue, income, you need to complete 5 steps.

And the second will appear in the profit and loss statement - cost price under the contract. This line is also called expenses for the main type of activity. In the company's practice, this line is also called cost price of sales. And this cost price of sales is recognized, like revenue. Either in a certain period of time, or over a certain period of time. And here the rules are as follows: if you recognize revenue at one time, then the cost of sales must be recognized at one time. If you recognize revenue over a long period of time, then the cost of sales must be recognized over this long period of time. As a consequence, in the second option, when we recognize revenue and cost over a long period of time, the first and second indicators are calculated based on the percentage of work completed. Thus, the indicators reflected in the financial statements of the company, related to the formation of revenue in the financial statements are the following:

The Profit and Loss Statement reflects the following indicators:

-Revenue (based on the 5 steps listed above)

-Cost (expenses) under the contract (recognized at a certain point in time or over a certain period of time).

If we are talking about the financial position report, then as a result of the sale of goods, works and services, then it will contain a fairly large number of indicators. In particular, our first indicator is accounts receivable. When do we have it? If you have shipped products or provided services, and the buyer has not yet paid for these products. That is, he owes the company, and therefore accounts receivable appear. The following point is important: if the seller company received cash, then instead of accounts receivable, cash will be reflected in the corresponding line in the financial position report.

The second indicator of the financial position statement is capitalized costs. When a company carries out long-term production or performs a long-term contract, it begins to produce goods, works and services and capitalize the costs of work in progress. So those costs that have not yet turned into cost of sales are reflected in the financial position report. Subsequently, when

these works or services are performed, these costs turn into the second line of the profit and loss report.

The third and fourth indicators are the so-called calculated indicators. There is such a concept as an asset under a contract or obligations to be performed under a contract. In the first case, we are talking about the amount that is due to the customer under the contract, and in the second case, we are talking about the amount that is subject to execution under this contract.

Why are these indicators calculated? In fact, they only arise if the company reflects revenue based on the percentage of work completed. And the percentage of work completed, as we have seen in the previous examples, is a calculated indicator. And very often a situation arises when a company actually incurred costs greater than those reflected in the profit and loss statement, and when invoicing a customer, it overstates this amount and the customer, as it were, pays for future work and services in advance in the current period. In this situation, the manufacturing company remains indebted to the buyer and this will be an obligation to fulfill. If the buyer company pays a smaller amount in the interim payments than the manufacturer company has incurred in costs, taking into account its financial results, then the buyer remains indebted under this agreement and this calculated amount is called an asset under the agreement.

Thus, the following indicators are reflected in the Statement of Financial Position:

- Accounts receivable under the contract (in the amount of recognized revenue)
- Capitalized costs (costs of work in progress)
- Contract asset (amount due from the customer under the contract)
- Performance obligation (amount to be performed under the contract).

Conclusion. And so, summing up the current topic, revenue is income from the main type of activity. The concept of prudence, which is embedded in international standards, tells us that income cannot be overstated, it cannot be reflected until the moment of their actual receipt. Therefore, Standard 15 very clearly interprets all the steps that need to be taken to recognize revenue, clearly sets out the criteria for its recognition, in no case allowing this artificial overstatement of income.

If the company understands that the standards are being implemented and all the company's actions comply with standard 15, then the income from revenue will appear in the profit and loss statements, the cost price will appear. But also as a result, the company will be able to show its real financial result from the main type of activity.

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JOURNAL OF MULTIDISCIPLINARY SCIENCES AND INNOVATIONS

VOLUME 05. ISSUE 01
MONTHLY JOURNALS



ISSN NUMBER: 2751-4390

IMPACT FACTOR: 9,08

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