Recognition of revenue on freight forwarding services

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Introduction

Global Lanka Limited is a Limited liability company which is providing international freight forwarding services and clearing services.Exporters handover their goods to the company and the company transport to destination with the assistance of suppliers in the company. Currently,revenue and cost of revenue of the company were recognized without concerning whether it qualifies for recognition under relevant accounting standard and stage of completion at the time of reporting date by the company. According to the SLFRS for SMEs, Revenue from rendering service need to be recognized when stage of completion can be reliably measurable at the reporting date.

Discussion of the Issue

The normal forwarding transaction is carried out in four stages. The company assesses cost of each stage before accepting the contract and determines the sale price by adding a profit margin to it and confirms it with an agreement with customers (Exporters). Level of completion of each stage is followed on exchanging documents and via mails with their suppliers. But the issue is company recognizes revenue and cost of revenue before completing each stage and company can't measure stage of completion reliably due to the non-completion of each stage. (Example given below)

Invoice No	Stage 01	Com: %	Stage 02	Com: %	Stage 03	Com: %	Stage 04	Com: %
12 UKR	35,111.	100	325,600.	75	41,664	0	136,710	.0

(Com: - Completion %, Total Cost – Rs.539, 085.00)(Gross Profit Margin 8%, Total Revenue – Rs.582, 211.80)

In this case the company has recognized total cost and total revenue as company's cost of revenue and revenue end of the period. Although second stage is completed 75%, it can't be measured reliably. It is non-compliance with SLFRS for Small and Medium Enterprises. According to this scenario, the company has failed to recognize revenue & cost of revenue as at the reporting date accurately and it presents an incorrect gross profit in Statement of Comprehensive Income. On the other hand, computation of tax is not correct, and also management has failed to take a proper decision on revenue and profit for the period.

Conclusions and Recommendations

In this case, we can identify that only Rs.35, 111/- as cost of sale and 37,920/- (Cost +8%) as revenue at the reporting date. Balance cost of revenue (Rs.503, 974.00) & revenue (Rs.544, 292.00) should be reversed.

Revenue from rendering service need to be recognized when stage of completion can be reliably measurable at the reporting date as per the section 23.14-23.16 and 23.21-23.27 of SLFRS for Small and Medium Enterprises. Specially, the outcome of a transaction can be estimated reliably when four conditions are satisfied according to the standard.

We suggest to the client; Revenue should be recognized based on the stage of completion as at the reporting date and it can be *reliably measurable according to the SLFRS for Small and Medium Enterprises and further the system should be adjusted in a way to facilitate stage of completion* method.