

Accounting Impact of New Income Standards on Income Accounting of Construction Industry Enterprises

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Abstract. On July 5, 2017, China's Ministry of Finance issued the revised "Accounting Standards for Business Enterprises No. 14 – Revenue". One of the main amendments is to incorporate the original income criteria and construction contract criteria into a unified revenue recognition model. The new income standard has been gradually implemented since January 1, 2018. Once implemented, it will inevitably have a major impact on the accounting work of construction industry enterprises. Therefore, this paper analyzes the accounting impact of changes in new income standards on the income accounting of construction industry enterprises from three aspects of revenue recognition, measurement and disclosure.

1. Introduction

As one of the pillar industries of the national economy, the construction industry is engaged in the construction of social infrastructure and other facilities and other related activities. Its total output value is second only to agriculture and industry in the material production sector. The products produced by enterprises in this industry are usually large in size, long in cycle, high in value, and non-replicable. Compared with the production activities and management methods of general industrial enterprises, there is a big difference in accounting, which leads to its particularity in the accounting of income. In 2006, the Ministry of Finance promulgated the "Enterprise Accounting Standards No. 14 - Revenue" and "Enterprise Accounting Standards No. 15 - Construction Contracts", which defined the normative requirements for the accounting of income from construction industry enterprises (hereinafter referred to as "construction enterprises"). In 2017, the Ministry of Finance made a major revision to the "Accounting Standards for Business Enterprises No. 14 – Revenue" (hereinafter referred to as the "New Income Standards"), and incorporated the current construction contract criteria into a unified measurement model with income standards. The promulgation of the new income standard has caused changes in the accounting of income of construction enterprises. What specific impacts these changes have on the accounting results of enterprises, and thus the changes in the relevant information provided by the financial statements of enterprises need to be carefully studied.

2. Changes in the income accounting of construction industry enterprises under the new income standard

2.1 Change in revenue recognition time

Since the building products are usually real estate, the product is large in size, fixed in position, and has a long production cycle. It often requires cross-year construction. The construction company usually signs an irrevocable construction contract with the customer in advance and carries out product construction in accordance with the contract. Therefore, the construction contract guidelines stipulate that, on the balance sheet date, if the outcome of the construction contract can

be reliably estimated, the construction company will use the percentage of completion method to confirm the revenue over a period of time according to the completion schedule. There are three methods for determining the completion schedule: (1) determining the proportion of the contractual cost actually completed according to the estimated total cost of the contract; (2) determining the proportion of the contracted workload that has been completed to the estimated total workload of the contract; When the ratio determined by the above two methods is not available, it can also be determined according to the actual progress of the measurement. As can be seen from the above regulations on contract revenue recognition, the income of construction enterprises is generally confirmed gradually according to the completion progress within a period of time (ie during construction period), and the completion schedule is the percentage of completed or completed work.

The new income standard stipulates that the recognition of income over a period of time needs to meet one of the following three criteria: (1) the customer obtains and consumes the economic benefits brought by the performance of the enterprise while the company is performing; (2) the customer can control Commodities under construction during the performance of the enterprise; (3) The goods produced during the performance of the enterprise have irreplaceable uses, and the enterprise has the right to receive payment for the part of the performance that has been completed so far throughout the contract period. If the above standard requirements are met, the company will recognize the income according to the progress of the contract during the period, and the performance of the performance will be determined by the output method or the input method. Among them, the output method is based on the value of the goods transferred to the customer to determine the progress of the performance, that is, similar to the percentage of completed work; the input method is to determine the progress of the performance based on the input of the company to fulfill its performance obligations. that is, similar to the percentage of completed costs. When the performance of the performance cannot be reasonably determined, if the costs incurred by the enterprise are expected to be compensated, the revenue shall be recognized according to the amount of costs incurred, until the performance of the performance can be reasonably determined. However, the new income standard also stipulates that if one of the above three items is not met, the income should be confirmed at a certain point in time. That is to say, the income of the construction company may not be confirmed gradually according to the completion progress within a certain period of time, but is confirmed at a certain point in time.

2.2 Changes in income measurement standards

The construction enterprise is mainly engaged in the construction and installation engineering construction business. It signs the construction contract with the contractor in advance and carries out the construction work according to the construction contract. The income source of the enterprise is usually the construction contract income. The construction contract guidelines clarify the specific content of the contract revenue, including the initial income specified in the contract and the income generated by contract changes, claims, awards, etc. From the specific terms of the construction contract standard, only the content of contract revenue and the confirmation of contract revenue are stipulated, but there is no clear standard for the measurement of contract revenue. Therefore, the basis for measuring contract revenue in accounting is the relevant provisions in the income standard. Relevant provisions, "Enterprises shall determine the total amount of income in accordance with the contract or agreement price received or receivable, except that the contract or agreement price received or receivable is not fair," that is, the construction contract income shall be measured according to the fair value of the consideration received or receivable.

The new income standard stipulates that an enterprise shall measure income according to the transaction price allocated to each individual performance obligation, that is, the income measured by fair value is revised to measure income at the transaction price. According to the interpretation of the new income standard, the transaction price refers to the amount of consideration that the enterprise is expected to receive due to the transfer of goods to the customer. At the same time, the new income standard provides guidance for companies to measure how complex transactions are

conducted, emphasizing that companies should determine transaction prices based on contractual terms and in combination with their previous practices. When determining the transaction price, the enterprise should consider the impact of variable consideration, major financing components in the contract, non-cash consideration, and customer consideration. That is to say, the construction contract revenue of the construction enterprise is further expanded, including not only the variable consideration caused by contract changes, claims, awards, etc., but also the major financing nature, non-cash payment and customer consideration.

2.3 Changes in income information disclosure

The construction contract standard stipulates that the enterprise shall disclose the four aspects related to the construction contract, namely the total amount of the contract and the method for determining the progress of the completion; the cumulative cost of the contract, the accumulated gross profit (or loss); the amount of the settlement price The reason and amount of the expected loss for the current period. According to the new income standard, companies need to disclose the following in their reports: accounting policies used for revenue recognition and measurement, judgments and changes that have a significant impact on the timing and amount of revenue recognition; and contract-related information, mainly Including information on revenue recognition in the current period, accounts receivable, contract asset contract liability balance and change information, performance obligation related information, how the transaction price is distributed to the performance obligation information; related to the assets determined by the contract cost capitalization Information; information on the long-term payment period without considering its significant financing components and expenseized contract cost information, etc.

3. Accounting impact of changes in income accounting of construction industry enterprises under the new income standard

3.1 Accounting impact of changes in revenue recognition

3.1.1 May delay the confirmation of revenue

According to the construction contract guidelines, the income of construction companies is usually gradually confirmed by the completion schedule during the construction period, and the new income standard emphasizes that if one of the three criteria is not met, the income should be confirmed at a certain point in time. It is basically close to the completion point of the construction contract. This makes it impossible for all construction contracts to use the percentage of completion method to gradually confirm the income after the construction company implements the new income standard. Instead, the construction contract must be identified first, and only if the standard requirements are met, in order to achieve a gradual confirmation of contract revenue . As a result, the construction company has to wait until the contract is completed to confirm the contract revenue due to the unsatisfied conditions of the transfer of control rights, which leads to the delay of the enterprise revenue confirmation time.

3.1.2 May cause revenue recognition to be out of touch with actual cash flow

According to the construction contract standard, the construction enterprise gradually confirms the income during the construction period according to the completion percentage method according to whether the risk reward is transferred. At the same time, the construction price is settled according to the construction progress. This is because the construction contract usually stipulates that payment should be made according to the construction schedule, which can alleviate the construction pressure of the construction enterprises. The new income standard incorporates the construction contract criteria into the measurement model that is consistent with the income standard, so that the judgment of the revenue recognition point does not lie in the nature of the transaction business, and the key lies in the fulfillment of the performance obligation of the enterprise. Once the construction company needs to confirm the income at the time of completion, this will result in the inconsistency between the inflow time of the project and the confirmation time of the enterprise revenue.

3.2 Accounting impact of changes in income measurement standards

3.2.1 *Uncertainty in reducing the amount of income that can be measured by fair value*

The new income standard pays more attention to contract awareness. The measurement of income is based on contract, and the income of the enterprise is measured at the transaction price, that is, the amount that is expected to be charged according to the transfer of goods for the customer. At the same time, it has made clear guidance on the variable consideration, major financing components and non-cash considerations involved in the transaction price. The measurement of income under the new income standard is not affected by changes in market prices, and in most cases is the contract price received or receivable. But it is not fixed, but a variable amount that varies due to discounts, rebates, refunds, incentives, performance bonuses, etc. In this way, enterprises are easier to identify and grasp, and to some extent, they avoid the many disadvantages that fair value measurement may be affected by a variety of uncertain external market changes.

3.2.2 *It can reduce the inappropriate amount of the variable consideration to cause the amount of income measurement*

Due to the long-term production of building products, the longer the construction period, the greater the possibility of encountering uncertain factors in the construction process, and the more impact on the construction contract. Therefore, the variable consideration contract is a common type of business in the construction industry, for example Contract changes, claims or awards, etc. may result in variable consideration. In the construction contract standard, the construction enterprise cannot arbitrarily confirm the measurement of the income amount due to the change of the income due to contract changes, claims, rewards, etc, only when this part of the income is recognized by the customer and the amount can be reliably measured can it be included in the total contract revenue. But there is no clear definition of how to make a reliable measurement. In the new income standard, the variable consideration in the contract clearly defines its measurement method, that is, according to the expected value or the most likely amount, the amount that best reflects the company's expected entitlement is determined; It can be recognized as the upper limit of the amount of income, that is, the transaction price including the variable consideration does not exceed the amount that the accumulated recognized income is unlikely to be significantly reversed when the relevant uncertainty is eliminated. The new income standard's clarification of the variable consideration measurement method in contract revenue and the improvement of measurement standards not only provide application guidelines for enterprises, but also further emphasize the accuracy and prudence in revenue recognition.

3.2.3 *Can improve the amount of income measurement caused by major financing components*

Due to the long construction period of construction projects, coupled with the huge cost of construction, the settlement of construction products and engineering prices of construction products usually need to be carried out in stages according to certain objective laws. Therefore, settlement of engineering prices and contract revenue Accounting has also become a long-term accounting act. In the construction contract standard, there is no clear definition of the long-term payment calculation formed by the construction contract. The construction companies generally do not strictly distinguish whether they need to treat the advance payment or receivables as long-term funds, and will not consider their time value. In the new income standard, the time interval between the time when the customer expects to obtain control of the commodity and the price paid by the customer is regarded as the criterion for determining whether the contract price of the enterprise is the financing behavior. For time intervals greater than one year, there is a significant financing component of the contract price, and the impact of the time value of money on income should be considered. That is to say, the new income standard has specific provisions for the existence of significant financing components in terms of revenue recognition time and the time interval between settlement of accounts receivable or receivables, the construction enterprise shall measure the transaction price according to the assumed transaction price of the contractor when the commodity control right is obtained, and the difference between the transaction price and the contract price shall be amortized by the actual interest rate method during the contract period. If the construction enterprise confirms that the income time is earlier than the contractor pays the

construction cost for more than one year, the revenue shall be recognized according to the transaction price measured at the present value, and the unrealized financing income shall be confirmed, and the corresponding financial expenses shall be offset; if the enterprise confirms the income. If the time is later than the company's inflow time of more than one year, the financial expenses and unrecognized financing expenses shall be confirmed, and the income measurement amount shall be adjusted when the income is recognized. In this way, regardless of whether the long-term payment is received in advance or deferred, the amount of income measurement is the same as the amount of income calculated according to the performance obligation, which can improve the problem that the income measurement amount is different due to the different settlement time of the engineering price.

3.3 Accounting impact of changes in income information disclosure

3.3.1 Refine the content of income information disclosure

Comparing the requirements for the disclosure of information, it can be found that the requirements of the new income standard are much higher than the requirements of the construction contract. The construction contract guidelines are only four simple items listed in the disclosure chapter. The original income standard requires less disclosure of income information. It only requires disclosure of the accounting policies used for revenue recognition and the amount of income recognized in the current period. The requirements for disclosure of income information in the new income standard far exceed the disclosure requirements of the construction contract standard and the original income standard. From the content of the disclosure requirements, the information related to income disclosure is much more complicated and detailed. It not only requires disclosure of accounting policies related to revenue recognition and measurement, but also requires disclosure of the specific details of the operational methods and nature involved in the revenue recognition and measurement process. In general, the construction contract standard focuses on the disclosure of income results, the disclosure is relatively simple, and the new income standard requires disclosure for the entire process of income generation, refining the disclosure requirements for income-related information, disclosure information is more specific.

3.3.2 Increased the difficulty of information disclosure

The methods of revenue recognition and income measurement in the new income standard have undergone tremendous changes. Only by truly understanding and mastering the essence of the income standard can the disclosed income information meet the corresponding disclosure requirements, which is puts high demands on the professional quality and business adaptability of accountants. For the accounting staff of construction companies, this kind of work is more difficult. Because it is necessary to identify the construction contract with long cycle and high volatility, the determination of the transaction price in the construction contract, the identification of the contract performance obligation and the determination of the progress of the contract, etc., all require very strong professional knowledge.

In general, the new revenue standard integrates the construction contract standard and the income standard into a confirmation model, which solves the inconsistency of revenue recognition and measurement methods caused by different construction business types and contract requirements of construction enterprises, and improves the quality of enterprise income information. Therefore, it is beneficial to enhance the application value of accounting information.

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