

Construction Contracts
Illustrative Examples

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These illustrative examples accompany, but are not part of, SB-FRS 11.

Disclosure of accounting policies

The following are examples of accounting policy disclosures:

Revenue from fixed price construction contracts is recognised on the percentage of completion method, measured by reference to the percentage of labour hours incurred to date to estimated total labour hours for each contract.

Revenue from cost plus contracts is recognised by reference to the recoverable costs incurred during the period plus the fee earned, measured by the proportion that costs incurred to date bear to the estimated total costs of the contract.

The determination of contract revenue and expenses

The following example illustrates one method of determining the stage of completion of a contract and the timing of the recognition of contract revenue and expenses (see paragraphs 22–35 of the Standard).

A construction contractor has a fixed price contract for 9,000 to build a bridge. The initial amount of revenue agreed in the contract is 9,000. The contractor's initial estimate of contract costs is 8,000. It will take 3 years to build the bridge.

By the end of year 1, the contractor's estimate of contract costs has increased to 8,050.

In year 2, the customer approves a variation resulting in an increase in contract revenue of 200 and estimated additional contract costs of 150. At the end of year 2, costs incurred include 100 for standard materials stored at the site to be used in year 3 to complete the project.

The contractor determines the stage of completion of the contract by calculating the proportion that contract costs incurred for work performed to date bear to the latest estimated total contract costs. A summary of the financial data during the construction period is as follows:

	Year 1	Year 2	Year 3
Initial amount of revenue agreed in contract	9,000	9,000	9,000
Variation	–	200	200
Total contract revenue	<u>9,000</u>	<u>9,200</u>	<u>9,200</u>
Contract costs incurred to date	2,093	6,168	8,200
Contract costs to complete	<u>5,957</u>	<u>2,032</u>	–
Total estimated contract costs	<u>8,050</u>	<u>8,200</u>	<u>8,200</u>
Estimated profit	950	1,000	1,000
Stage of completion	26%	74%	100%

The stage of completion for year 2 (74%) is determined by excluding from contract costs incurred for work performed to date the 100 of standard materials stored at the site for use in year 3.

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The amounts of revenue, expenses and profit recognised in the statement of comprehensive income in the three years are as follows:

	To date	Recognised in prior years	Recognised in current year
Year 1			
Revenue (9,000 × .26)	2,340	–	2,340
Expenses (8,050 × .26)	<u>2,093</u>	<u>–</u>	<u>2,093</u>
Profit	<u>247</u>	<u>–</u>	<u>247</u>
Year 2			
Revenue (9,200 × .74)	6,808	2,340	4,468
Expenses (8,200 × .74)	<u>6,068</u>	<u>2,093</u>	<u>3,975</u>
Profit	<u>740</u>	<u>247</u>	<u>493</u>
Year 3			
Revenue (9,200 × 1.00)	9,200	6,808	2,392
Expenses	<u>8,200</u>	<u>6,068</u>	<u>2,132</u>
Profit	<u>1,000</u>	<u>740</u>	<u>260</u>

Contract disclosures

A contractor has reached the end of its first year of operations. All its contract costs incurred have been paid for in cash and all its progress billings and advances have been received in cash. Contract costs incurred for contracts B, C and E include the cost of materials that have been purchased for the contract but which have not been used in contract performance to date. For contracts B, C and E, the customers have made advances to the contractor for work not yet performed.

The status of its five contracts in progress at the end of year 1 is as follows:

	A	B	C	D	E	Total
Contract revenue recognised in accordance with paragraph 22	145	520	380	200	55	1,300
Contract expenses recognised in accordance with paragraph 22	110	450	350	250	55	1,215
Expected losses recognised in accordance with paragraph 36	–	–	–	40	30	70
Recognised profits less recognised losses	35	70	30	(90)	(30)	15
Contract costs incurred in the period	110	510	450	250	100	1,420
Contract costs incurred recognised as contract expenses in the period in accordance with paragraph 22	110	450	350	250	55	1,215
Contract costs that relate to future activity recognised as an asset in accordance with paragraph 27	–	60	100	–	45	205
Contract revenue (see above)	145	520	380	200	55	1,300
Progress billings (paragraph 41)	100	520	380	180	55	1,235
Unbilled contract revenue	45	–	–	20	–	65
Advances (paragraph 41)	–	80	20	–	25	125

The amounts to be disclosed in accordance with the Standard are as follows:

Contract revenue recognised as revenue in the period (paragraph 39(a))	1,300
Contract costs incurred and recognised profits (less recognised losses) to date (paragraph 40(a))	1,435
Advances received (paragraph 40(b))	125
Gross amount due from customers for contract work – presented as an asset in accordance with paragraph 42(a)	220
Gross amount due to customers for contract work – presented as a liability in accordance with paragraph 42(b)	(20)

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The amounts to be disclosed in accordance with paragraphs 40(a), 42(a) and 42(b) are calculated as follows:

	Contract					Total
	A	B	C	D	E	
Contract costs incurred	110	510	450	250	100	1,420
Recognised profits less recognised losses	<u>35</u>	<u>70</u>	<u>30</u>	<u>(90)</u>	<u>(30)</u>	<u>15</u>
	145	580	480	160	70	1,435
Progress billings	<u>100</u>	<u>520</u>	<u>380</u>	<u>180</u>	<u>55</u>	<u>1,235</u>
Due from customers	45	60	100	–	15	220
Due to customers	–	–	–	(20)	–	(20)

The amount disclosed in accordance with paragraph 40(a) is the same as the amount for the current period because the disclosures relate to the first year of operation.