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When to recognise revenue on services provided

Revenue recognition often causes confusion among contractors and subcontractors, but it is essential to get it right to avoid HMRC investigations. Construction contracts can often span several months and reporting periods. Let's take a look at how construction workers should recognise revenue.

Work in progress

Work in progress (WIP) is a way of recording income before a job has been invoiced. Since income and corresponding expenses often don't occur in the same period, it's important to recognise the progress of contracts within a reporting period or tax year, if applicable.

When you can reliably estimate how much money you will earn from a contract, you should **recognize that income as it becomes available.** This means that if you have completed most of the work but have not yet been paid, you should still count that income in your financial reports.

In other words, it should be recognised gradually, based on the stage of completion of the transaction at the end of the reporting period.

According to The International Accounting Standard IAS 18, the transaction can be estimated reliably when all the following conditions are met:

- The amount of revenue can be measured reliably.
- It is probable that the economic benefits associated with the transaction will flow to the seller.
- The stage of completion of the transaction at the end of the reporting period can be measured reliably.
- The costs incurred to date for the transaction and the costs to complete the transaction can be measured reliably.

If it's not possible to reliably measure the outcome of a job, then you can only recognise revenue up to the amount of money that was spent to provide the service.

Determining the stage of completion

Although there are no set rules for calculating the stage of completion of a project, some common methods include:

- Comparing the costs incurred to date to the total contract cost.
- Comparing the services performed to date to the total services to be performed.
- Surveys of work performed.

It would be beneficial to prepare a Cost Value Reconciliation (CVR) or Cost Value Comparison (CVC) report to show the value of the work completed to date as well as the profit.

Example

For example, a contractor has a job worth £200,000. The estimated total budget is £150,000. If the costs incurred to date are £30,000, the contractor will divide the costs incurred by the estimated budget (£30,000/£150,000 = 0.2). Therefore, the percentage of the job completed is 20%.

By multiplying the percentage of the job completed by the contract amount (0.2 x £200,000), the amount that should have been billed to date is £40,000.

This is one way to calculate the stage of completion. If you would like to learn more about this, please contact us.