

Name of Publisher: BRIGHT EDUCATION RESEARCH SOLUTIONS

Area of Publication: Business, Management and Accounting (miscellaneous)



Let's Start!

Journal of Management & Social Science

ISSN Online: 3006-4848

ISSN Print: 3006-483X

<https://rjmss.com/index.php/7/about>

RECOGNIZED IN "Y"
CATEGORY BY



[Revenue Recognition and Credit Risk Assessment under IFRS And US GAAP: Distinctions and Practical Challenges in the Middle East Market]

Syed Safwan Kamal

FCCA, FCA, MiF. safwan_kamal@hotmail.com

Dr. Shah Hussain Awan

Lecturer, Abdul Wali Khan University, Mardan. shah.awan@awkum.edu.pk

Review Type: Double Blind Peer Review

ABSTRACT

The distinction between project performance issues and credit deterioration is one of the most complex aspects of revenue recognition and receivables accounting. This paper examines the treatment of uncollectible amounts under International Financial Reporting Standards (IFRS) and US Generally Accepted Accounting Principles (US GAAP), highlighting the importance of proper classification, presentation, and disclosure. It further explores the implications for businesses operating in the Middle East, where commercial practices and payment behaviors create unique challenges for accountants and auditors. Drawing on recent guidance and examples, this analysis offers practical recommendations for controllers, finance teams, and external auditors to ensure compliance and enhance financial statement transparency.

Keywords: IFRS 15, IFRS 9, ASC 606, ASC 310, Revenue Recognition, Expected Credit Losses, Bad Debt Provision, Receivables Impairment, Credit Deterioration, Revenue Adjustments.

Introduction

In today's dynamic corporate landscape, delayed customer payments have become a growing concern for companies across various industries. This challenge is particularly acute in the Middle East, where complex contractual structures, cultural practices surrounding payment timelines, and recent economic uncertainties have compounded the issue. In such environments, finance professionals must carefully assess whether outstanding receivables stem from performance-related deficiencies or from the declining creditworthiness of clients. This distinction is critical, as it not only influences revenue recognition decisions but also impacts perceptions of a firm's financial health and risk management practices.

Although both IFRS and US GAAP provide comprehensive guidance on revenue recognition and credit risk assessment, their practical implementation demands a thorough understanding of performance obligations, enforceable rights, and the financial status of customers. This study explores the conceptual and procedural distinctions between the two accounting standards, highlighting illustrative journal entries, disclosure requirements, and real-world challenges unique to the Middle Eastern context. It also offers practical recommendations to enhance compliance and financial governance in the region (Deloitte, 2022).

Distinction Between Contract Assets & Receivables

Before delving into the detailed analysis of revenue recognition and credit risk treatment, it is important to clarify a foundational point regarding the classification of receivables and unbilled amounts under both IFRS and US GAAP. In practice, the terms "unbilled receivables," "contract assets," and "trade receivables" are often used interchangeably, which can lead to confusion when assessing the appropriate accounting treatment for reversals and impairment.

The distinction between contract assets and receivables is critical because it influences not only the balance sheet presentation but also the timing of revenue recognition and the assessment of collectability.

The following section briefly outlines how these concepts are defined within the

Journal of Management & Social Science

VOL-2, ISSUE-3, 2025

respective frameworks and how companies should determine whether an unbilled balance qualifies as a contract asset or an unconditional receivable.

Under IFRS 15, a contract asset arises when an entity has a right to consideration in exchange for goods or services that have already been transferred to the customer, but the entitlement to payment is conditional on something other than merely the passage of time. For example, this could occur when the receipt of payment depends on achieving certain future performance milestones. In contrast, a receivable represents a right to consideration that is unconditional except for the passage of time. This means the entity has billed the customer or otherwise has an enforceable right to payment, and no further performance obligations or contingencies must be met before the payment is due.

Unbilled amounts are usually presented as contract assets if your right to payment is still conditional on performance obligations or customer acceptance. For example, if you have performed work but not yet billed because the final milestone or customer certification has not occurred; then it is a Contract Asset. In contrast, if you have performed work, no further performance obligations remain, and you simply haven't issued the invoice; then it is classified as a Receivable even though it is unbilled (Deloitte, 2023).

Many companies colloquially call both "unbilled receivables," but under IFRS 15 they must be classified properly as either contract assets or receivables depending on whether the right to payment is conditional.

Under US GAAP Accounting Standards Codification (ASC 606), the concept is essentially the same as under IFRS 15. A contract asset represents unbilled amounts for which payment depends on something other than merely the passage of time. In other words, additional conditions such as further performance or customer acceptance must still be satisfied before the right to payment becomes unconditional. Conversely, a receivable reflects an unconditional right to payment, where only the passage of time and the issuance of an invoice are necessary for collection (Malhotra, 2025).

Example from ASC 606: "An entity shall recognize a receivable when it has an unconditional right to consideration... A right to consideration is unconditional if only the passage of time is required before payment is due." So, Unbilled amounts = contract assets if the right to payment is conditional.

To distinguish between a receivable and a contract asset, consider whether the right to payment is unconditional. If the only remaining step is billing and the passage of time, the amount is a receivable. If payment depends on further milestones, performance obligations, or customer approvals, it qualifies as a contract asset. Not all unbilled amounts are contract assets; the correct classification depends on whether the right to payment is conditional or unconditional.

IFRS Framework

Core Standards

Under IFRS, revenue recognition and receivables impairment are primarily addressed by two standards. IFRS 15: Revenue from Contracts with Customers sets out when and how revenue should be recognized, requiring that revenue be recorded only when control of goods or services has been transferred to the customer. IFRS 9: Financial Instruments governs the classification, measurement, and impairment of financial assets, including

Journal of Management & Social Science

VOL-2, ISSUE-3, 2025

trade receivables. It requires companies to estimate and recognize expected credit losses (ECL) even before a default occurs. In essence, IFRS 15 determines the timing and amount of revenue recognition, while IFRS 9 ensures that receivables are measured net of any anticipated credit losses.

Performance Issues vs. Credit Deterioration

The crucial question is whether the amounts billed or unbilled are not recoverable due to performance issues or due to credit deterioration. If the amounts are not collectible because the entity has failed to satisfy a performance obligation or the contract is in dispute, revenue must be reduced, as it was never actually earned. On the other hand, if the amounts are not recoverable because the customer is unable to pay for reasons unrelated to the entity's performance; for example, due to credit deterioration then the revenue remains recognized, and an impairment loss is recorded to reflect the expected credit loss.

This distinction aligns with IFRS 15.47, which requires companies to reassess variable consideration and adjust revenue when it is probable that a significant reversal will occur, versus IFRS 9.5.5.17, which governs lifetime expected credit losses when credit risk has increased significantly (EY, 2023).

Journal Entries

Scenario A – Project Performance Issue. When revenue is reversed due to project performance problems:

DR Revenue (PCL)

CR Billed/Unbilled Receivables (Balance Sheet)

This entry aligns the receivable reduction with revenue reduction, ensuring no understatement of impairment losses or overstatement of revenue.

Scenario B – Credit Deterioration. When revenue is earned but becomes uncollectible: DR Impairment Loss (Operating Expenses/SGCA)

CR Allowance for Expected Credit Losses (Balance Sheet)

Here, revenue remains unchanged, reflecting that the contractual right to consideration arose from satisfying performance obligations.

Presentation and Disclosure

IFRS 7 requires disaggregation of impairment losses and disclosure of credit risk management policies, inputs, and assumptions used to measure ECL. Importantly, impairment losses are presented separately within operating expenses and not netted against revenue.

For example, a Middle East construction company with significant trade receivables arising from long-term projects must provide specific disclosures. These include details of changes in loss allowances, reconciliations of the opening and closing balances of those allowances, and narrative descriptions explaining the estimation techniques applied to measure expected credit losses.

Middle East Considerations

In the Gulf Cooperation Council (GCC) region, several factors complicate the assessment of trade receivables and credit risk. Many construction and services contracts involve complex terms, including variable consideration and milestone based payments, which can make revenue recognition more challenging. Extended payment terms are also common, as cultural norms often tolerate longer delays than in Western markets, requiring

Journal of Management & Social Science

VOL-2, ISSUE-3, 2025

companies to carefully evaluate whether such delays truly indicate credit risk. Additionally, many customers are quasi-governmental entities whose payment practices and timelines differ significantly from those of private sector clients. Finally, currency fluctuations and liquidity pressures, often linked to movements in oil prices, can further influence payment behaviors and the overall credit environment (Rahman et al., 2025).

Companies operating in the Middle East should adopt robust processes to manage credit risk effectively. They should document the precise reasons for payment delays to clearly distinguish between issues related to performance and those stemming from other factors. It is also essential to obtain evidence demonstrating whether contractual obligations have been fulfilled or not. Regular monitoring of counterparties' financial health helps identify emerging credit concerns early. Additionally, finance teams should be trained to differentiate between culturally common payment delays and genuine signs of credit deterioration to avoid misclassifying receivables and to ensure appropriate accounting treatment.

US GAAP Framework

Core Standards

Under US GAAP, two key standards set out the requirements for revenue and receivables. ASC 606: Revenue from Contracts with Customers introduced a comprehensive model based on the transfer of control and a five-step process for recognizing revenue. It defines when and how much revenue should be recognized as contractual obligations are fulfilled. ASC 310-10: Receivables addresses the accounting for receivables, including their initial recognition, measurement, assessment of collectability, and the recording of allowances for credit losses. Together, these standards ensure that revenue is appropriately recognized and that receivables are measured to reflect expected credit risk.

Performance Issues vs. Credit Deterioration

The distinction under US GAAP is similar in principle to IFRS. If the entity has not satisfied its performance obligations or the contract is in dispute, any previously recognized revenue should be reversed, as it was never earned. In contrast, if the entity has fulfilled its obligations but collection has become unlikely due to credit deterioration, revenue remains recognized, and an allowance for doubtful accounts should be recorded to reflect the expected loss. This approach aligns closely with IFRS 15: Revenue from Contracts with Customers, which also differentiates between performance-related adjustments and credit risk impairments (Financial, 2012/13).

ASC 606-10-25-1 and 25-7 establish that revenue is recognized only when collection is probable, but once recognized, subsequent collection issues are treated under ASC 310.

Journal Entries

Scenario A – Project Performance Issues: DR

Revenue (PCL)

CR Billed/Unbilled Receivables (Balance Sheet)

Scenario B – Credit Deterioration:

DR Bad Debt Expense (Operating Expenses)

CR Allowance for Doubtful Accounts (Balance Sheet)

These entries mirror the IFRS treatment in principle but are subject to US GAAP-specific disclosure and presentation requirements.

Journal of Management & Social Science

VOL-2, ISSUE-3, 2025

Presentation and Disclosure

Under US GAAP, bad debt expense is presented within operating expenses, often classified under selling, general, and administrative expenses (SGCA). It is not netted against revenue. ASC 606-10-45-3 explicitly prohibits reducing revenue by credit losses. This requirement ensures that gross revenue and gross margin are reported transparently, providing a clear view of both the company's revenue-generating activities and the impact of credit risk separately.

Disclosures must include information about the accounting policy applied to credit losses, detailing how the company determines, and measures expected credit losses. Companies are also required to present changes in the allowance for doubtful accounts, showing the movements between opening and closing balances. Additionally, disclosures should explain the impact of credit losses on the financial results, helping users of the financial statements understand how credit risk affects overall performance.

Middle East Considerations

US multinationals with operations in the Middle East encounter additional complexities when applying US GAAP. Local payment practices often differ from expectations around timely collectability, making it harder to assess whether receivables should be considered impaired or unearned. Audit scrutiny has intensified, with US auditors increasingly requiring clear, documented evidence to justify judgments about collectability and revenue recognition. Furthermore, cross-border enforcement of overdue balances can involve significant legal and practical challenges.

To mitigate these risks, controllers should maintain contemporaneous evidence supporting revenue recognition decisions, prepare detailed reconciliations to facilitate management oversight and audit review, and clearly segregate project performance disputes from broader customer liquidity issues to ensure accurate financial reporting and compliance.

Practical Challenges and Recommendations

Determining the Root Cause of Nonpayment

The most significant challenge in practice is conclusively determining whether nonpayment results from performance issues or credit deterioration. Relying solely on payment history is not sufficient; the underlying reasons must be substantiated with clear evidence.

To address this, companies should require project managers to thoroughly document any contractual disputes and the status of performance milestones. Establishing regular credit reviews for customers who exceed agreed payment terms can help identify emerging risks early. Additionally, accounting staff should be trained to recognize that partial payments may coexist with disputes over specific invoices, ensuring that receivables are assessed accurately and classified appropriately.

Avoiding Misclassification in Financials

Misclassification of reversals has led to numerous audit findings. Recent audits in the Middle East have highlighted that companies often book the initial loss against revenue but then release the reserve through Selling, General & Admin (SGCA) expenses, or they net bad debt reversals against new impairment charges. These practices distort both gross margin and operating expense metrics, making it difficult for stakeholders to understand true

Journal of Management & Social Science

VOL-2, ISSUE-3, 2025

performance.

To address this, companies should enforce a clear policy requiring that any reversals be recorded to the same provision for credit losses line in the income statement, as the original booking. Additionally, implementing automated journal workflows can help prevent inappropriate netting of adjustments across different financial statement lines, ensuring consistency and transparency in reporting.

Governance and Internal Controls

Given the complexity and judgment involved, strong governance is essential to ensure accurate and compliant accounting. Best practices include conducting cross-functional reviews that bring together project teams, credit management, and controllership to evaluate receivables and related revenue recognition decisions collaboratively. Regular training should be provided to keep teams current on revenue recognition principles and emerging guidance. Additionally, centralized oversight of material receivables judgments helps promote consistency, improve documentation, and reduce the risk of errors or audit findings.

Conclusion

Revenue recognition and receivables impairment are areas of significant judgment and financial statement risk that demand rigorous attention from management. For companies operating in the Middle East, these challenges are amplified by cultural norms around extended payment timelines, the prevalence of complex contracts with milestone-based billing, and the involvement of quasi-governmental customers whose payment practices may differ substantially from private sector expectations. These factors create considerable ambiguity when assessing collectability and determining whether nonpayment arises from performance failures, contractual disputes, or genuine credit deterioration.

Both IFRS and US GAAP require companies to make clear, evidence-based conclusions about these issues, as the proper classification of receivables directly influences not only revenue and impairment accounting but also gross margins, operating expenses, and ultimately, the credibility of reported financial results. Missteps in this area can erode investor confidence, trigger audit findings, and result in restatements or regulatory scrutiny.

To navigate this complexity effectively, companies must invest in comprehensive training for project managers, credit teams, and accounting staff so that everyone understands the principles, documentation requirements, and judgment criteria involved. Robust internal controls, cross-functional governance processes, and systematic documentation of decisions are essential to support consistent, defensible accounting treatment. By prioritizing these measures, organizations can enhance transparency, strengthen stakeholder trust, and ensure compliance with both global and local reporting requirements.

References

Deloitte (2022). *Middle East CFO Survey*.

Deloitte (2023). *A Roadmap to Applying the New Revenue Recognition Standard (ASC 606)*.

Deloitte C Touche LLP.

EY (2023). *Applying IFRS: Revenue from Contracts with Customers (IFRS 15)*. Ernst C Young

Journal of Management & Social Science
VOL-2, ISSUE-3, 2025

Global.

Financial Accounting Standards Board (2014). ASC 606 Revenue from Contracts with Customers. FASB Codification.

Financial, S. Current Accounting Issues and Risks for Financial Management and Reporting– 2012/13.

IFRS Foundation (2014). IFRS 15 Revenue from Contracts with Customers. IFRS Standards.

Malhotra, P. (2025). Aligning Financial Reporting Standards. Aligning Financial Reporting Standards With Global Trade Needs, 153.

PricewaterhouseCoopers. Available at: www.pwc.com

PwC (2023). IFRS and US GAAP: Similarities and Differences.

Rahman, S. R. U., & Sabir, S. N. (2025). Sustainable practices, digital tools, and SME success: A pathway to long-term growth. *Policy Research Journal*, 3(3), 2025.