



Insights into IFRS 15

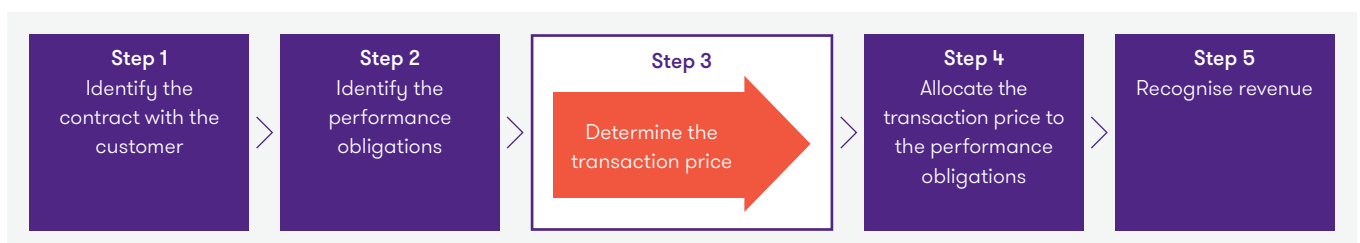
Determining the transaction price

For most entities, revenue is one of the most important indicators of performance. Ensuring revenue recognition principles are applied consistently and comparably across industries and capital markets is essential. IFRS 15 ‘Revenue from Contracts with Customers’ was developed through a joint initiative by the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) to enhance the quality of revenue reporting under both IFRS and US GAAP. While the Standard offers comprehensive guidance on revenue recognition, its detailed provisions can be complex and challenging for financial statement preparers to implement.

Our ‘Insights into IFRS 15’ series outlines the key aspects of the Standard, drawing attention to areas that are particularly difficult to apply in practice, with the aim of helping reporting entities better understand and implement IFRS 15’s requirements.

IFRS 15 introduced the five-step model for revenue recognition from contracts with customers.

This article deals with Step 3 of the five-step model, which covers determining the transaction price. For a full summary of the five-step model, refer to our article ‘[Insights into IFRS 15 – Overview and scope](#)’.



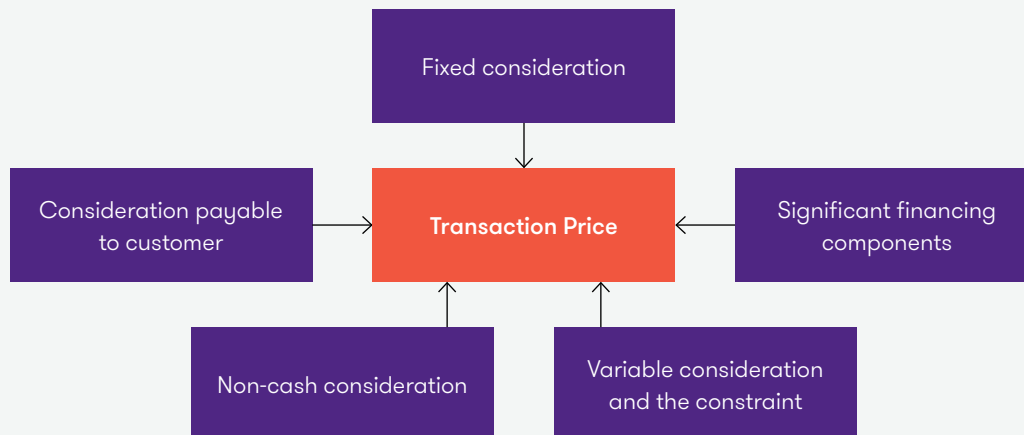
The objective of Step 3 is to predict the total amount of consideration to which the entity will be entitled from the contract.

The **transaction price** is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties.

The entity first identifies fixed consideration, including any non-refundable upfront payments. In addition to fixed consideration, the entity considers the effects of the following components in determining transaction price:

- **Variable consideration and the constraint**
- **Significant financing components**
- **Non-cash consideration**
- **Consideration payable to the customer**

Components for determining the transaction price



Variable consideration

When a contract includes a variable amount, the entity estimates the amount of variable consideration to which it expects to be entitled. This is because the transaction price is defined as the consideration an entity expects to be entitled to in exchange for transferring promised goods or services, which may include variable consideration. Variable consideration includes any consideration that is not fixed. In other words, the amount may fluctuate as a result of the outcome of uncertain events. Common examples of variable consideration include discounts, rebates, refunds, credits, bonuses, and penalties.

The variability may be explicitly stated in the contract or implicit (for example, based on the entity's business practices, the customer has a valid expectation that the entity will accept an amount of consideration that is less than the stated price in the contract). Variable consideration may be fixed in amount, but the entity's right to receive that consideration is contingent on future outcomes. For example, the amount of a performance bonus might be fixed, but because the entity is not entitled to that bonus until a performance target is met, the outcome is uncertain and therefore the amount is considered variable.

Estimating the amount of variable consideration

If a contract includes a variable amount, an entity estimates the variable part of the transaction price.

Practical insight – When is an entity not required to estimate variable consideration?

In limited situations, an entity may not be required to estimate the amount of variable consideration, including when the entity:

- is permitted to apply the right-to-invoice practical expedient (as discussed below)
- meets the allocation objective and is required to allocate variable consideration entirely to a distinct good or service that forms part of a series, or
- is required to apply the 'royalty exception' for a license of intellectual property.

The 'royalty exception' provides relief from estimating and constraining variable consideration when the variability relates to consideration tied to the sales and usage of intellectual property. However, the 'royalty exception' does not completely absolve the entity from all estimations.

Practical insight – Right-to-invoice practical expedient

When an entity is entitled to consideration from a customer that directly reflects the value delivered through its performance to date – such as in service agreements where billing is based on a fixed rate per hour of service rendered – the entity may recognise revenue equivalent to the amount it is entitled to invoice.

If an entity is permitted to apply the right-to-invoice practical expedient, the entity may not be required to estimate the amount of variable consideration.

To estimate the variable consideration in a contract, an entity determines either the expected value or the most likely amount of consideration to be received, depending on which method better predicts the amount to which the entity will be entitled. An entity may use different methods for different uncertainties in a single contract.

Example 1 – Estimating variable consideration

Construction Co. enters into a contract with a customer to build a manufacturing facility. The entity determines that the contract contains one performance obligation satisfied over time.

Construction is scheduled to be completed by the end of the eighteenth month for an agreed-upon price of CU 25 million.

The entity has the opportunity to earn a performance bonus for early completion as follows:

- 15% bonus of the CU 25 million contract price if completed by the fifteenth month (20% likelihood)
- 10% bonus if completed by the sixteenth month (50% likelihood)
- 5% bonus if completed by the seventeenth month (20% likelihood)

In addition to the potential performance bonus for early completion, Construction Co. is entitled to a quality bonus of CU 2 million if a health and safety inspector assigns the facility a gold star rating as defined by the agency in the terms of the contract. Construction Co. concludes that it is 80% likely that it will receive the quality bonus.

Analysis

In determining the transaction price, Construction Co. separately estimates variable consideration for each element of variability: the early completion bonus and the quality bonus.

Construction Co. decides to use the expected value method to estimate the variable consideration associated with the early completion bonus because there is a range of possible outcomes and the entity has experience with a large number of similar contracts that provide a reasonable basis to predict future outcomes.

Drawing from its past experience, Construction Co. identifies the following factors that could impact its ability to predict when the manufacturing facility will be completed:

- Completing projects with similar requirements in the same geographic region
- Working with the same subcontractors who completed similar construction projects ahead of schedule
- Relying on the same suppliers
- Performing in similar weather conditions

Therefore, the entity expects this method to best predict the amount of variable consideration associated with the early completion bonus. Construction Co.'s best estimate of the early completion bonus is CU 2,250,000, calculated as shown in the following table.

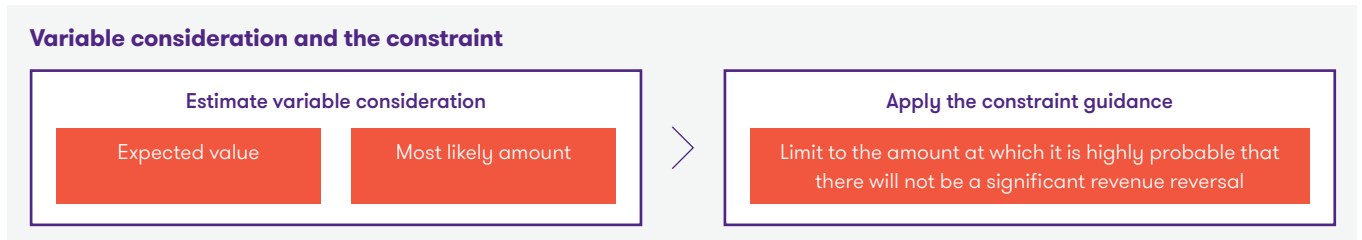
Possible bonus outcomes (CU)	Probability	Probability-weighted amount (CU)
3,750,000	20%	750,000
2,500,000	50%	1,250,000
1,250,000	20%	250,000
–	10%	–
		2,250,000

Construction Co. decides to use the most likely amount to estimate the variable consideration associated with the potential quality bonus because there are only two possible outcomes (CU 2,000,000 or CU nil) and this method would best predict the amount of consideration associated with the quality bonus. Construction Co. believes the most likely amount of the quality bonus is CU 2,000,000.

The entity next considers the guidance on constraining the estimates of variable consideration to determine whether it should include some or all of the estimates of variable consideration in the transaction price.

Constraint on variable consideration

If an amount of consideration in a customer contract is variable, an entity evaluates whether to constrain the amount of estimated variable consideration. The objective of the constraint is for an entity to recognise revenue only to the extent it is highly probable that a significant reversal in cumulative revenue recognised for the contract will not occur when the uncertainty is resolved. In other words, an entity includes some or all of its estimate of variable consideration in the transaction price to the extent that it is probable that a significant revenue reversal will not occur when the uncertainty leading to the variability is resolved.



Practical insight - Should the constraint be applied at the contract or performance obligation level?

IFRS 15 states that an entity should include in the transaction price some or all of an amount of variable consideration, but only to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognised will not occur when the uncertainty associated with the variable consideration is subsequently resolved. While the guidance does not specify at which level the assessment should take place (ie at the contract level or at the performance obligation level), the guidance might be read to suggest that the assessment takes place at the performance obligation level.

At its January 2015 meeting, the IASB and FASB joint Transition Resource Group for Revenue Recognition (TRG) members generally agreed with the FASB and IASB staff that the unit of account for determining the transaction price is the contract and not the performance obligation (TRG paper 14 on Variable consideration). While the guidance does not explicitly address the unit of account for the constraint guidance, the Basis for Conclusions of IFRS 15 does state that the unit of account for other considerations (namely identifying a significant financing component) is the contract level. Therefore, the TRG and staff generally agreed that entities should apply the constraint guidance at the contract level.

When determining the transaction price, an entity applies the constraint guidance at the contract level, rather than at the performance obligation level, before allocating the amounts to individual performance obligations.

Volume discounts

Tiered pricing clauses or volume discounts (hereafter referred to as 'volume discounts') are common in customer contracts. A volume discount means the price per good or unit of service changes (usually decreases) as the customer purchases an increased volume of goods or services. For example, an entity sells the first 1,000 units to a customer at CU 100 per unit, but any purchases in excess of 1,000 units are invoiced at CU 90 per unit. The accounting for volume discounts depends upon whether the volume discount results in retrospective price changes or only in prospective price changes.

Retrospective volume discounts

Contracts with retrospective volume discounts involve variable consideration, as the transaction price depends on the total volume of customer purchases. To determine the transaction price for a contract with a retrospective volume discount, the entity estimates the anticipated total purchase volume, applies the relevant pricing, and takes into account the constraint guidance.

Prospective volume discounts

An entity must evaluate contracts that include prospective volume discounts to determine if the discount provides the customer with a material right. This evaluation involves comparing the discount offered to similar customers that receive a discount independently of a prior contract with the entity.

If the entity determines that the discount offered to a customer for prospective purchases and the price offered to other similar customers, independent of a prior contract, are comparable, this may indicate that the price offered exists independently of the existing contract, and therefore the discount is not a material right.

If, however, the entity determines that the volume-based discount offered to the customer and the price typically offered to other similar customers independent of a prior contract are not comparable, this may indicate that a portion of the customer's payment at the earlier higher price (higher tier) is really just a prepayment for later purchases at a lower price (lower tier), ie the discount provides the customer with a material right which should be accounted for as a separate performance obligation.

Rights of return

Retailers and manufacturers often grant customers the right to return a product for a full or partial refund, credit, or an exchange for another product. This right of return can be explicitly stated in the contract or implicit within the customer agreement.

The exchange of a product for another 'identical' product is not considered a return, and is not subject to the guidance below. In addition, contracts that permit the exchange of a defective product for a functioning product should be evaluated using the warranty guidance.

Where a contract with a customer contains a right of return, an entity recognises revenue for these arrangements, net of estimated returns, as follows:

- Revenue for the sold products, reduced for estimated returns (the guidance on variable consideration applies to determine the amount of the estimated returns)
- A refund liability equal to the amount of consideration received that the entity expects to refund
- An asset initially measured at the carrying amount of the returned inventory, less costs of recovery, and a corresponding adjustment to cost of sales.

The entity should update its estimate of the refund liability at the end of each reporting period for any new information, with a corresponding adjustment to revenue.

A return right grants an entity the contractual ability to reclaim a good if a customer exercises the option to return it for a refund. This right is recognised as an asset and not offset against the refund liability. This separation enhances transparency and ensures that the asset is considered for impairment testing.

Distinguishing variable consideration from optional goods or services

It may be challenging to distinguish between a contract that contains an option to purchase additional goods and services and a contract that includes variable consideration based on variable quantities (such as a usage-based fee). This is an important distinction because of the difference in the accounting and disclosure requirements for options and variable consideration.

Practical insight - How can an entity distinguish between an optional purchase and variable consideration?

At its November 2015 meeting, the TRG reached general agreement that an entity needs to apply judgement to distinguish between contracts that contain an option to purchase additional goods or services and contracts that contain variable consideration.

The evaluation depends on the nature of the promise and what the enforceable rights and obligations are under the existing contract. For example, a contract obligates the vendor to transfer the promised goods or services and the customer to pay for those goods or services. If future customer actions or events result in additional consideration as or after control is transferred, this is an indication that the contract contains variable consideration. In this case, the customer's actions do not obligate the entity to transfer additional distinct goods or services.

Alternatively, an indication that a contract contains an option for additional goods and services is when the customer has a present contractual right to choose the amount of additional distinct goods or services that are purchased (ie it is a separate purchasing decision). Before the customer exercises that right, the vendor is not obligated to provide those goods or services. Instead, the customer's action in an optional purchase results in a new obligation for the vendor to transfer additional distinct goods or services.

The examples below, set out in TRG Paper 48, 'Customer options for additional goods and services', assist in distinguishing between variable consideration and an option to purchase additional goods or services.

Example of variable consideration

A transaction processor enters into a 10-year agreement with a customer to provide continuous access to its system and to process all transactions on behalf of its customer. The customer is obligated to use the transaction processor's system to process all of its transactions and is charged on a per transaction basis; however, the ultimate quantity of transactions is not known and remains outside the control of both the transaction processor and the customer. The customer simultaneously receives and consumes the benefit of the system and, therefore, the entity recognises revenue over time.

In the above case, the customer does not control the number of transactions processed and the nature of the promise is to provide the customer with continuous access to the processing platform. Because the transaction processor is already obligated to provide continuous access to the platform, the events that result in additional payment do not result in an obligation to transfer additional goods or services, which indicates that the contract includes variable consideration instead of a customer option.

Example of an option to purchase additional goods or services

A supplier enters into a five-year exclusive Master Service Agreement (MSA) with a customer, which obligates the supplier to produce and sell customised parts as requested by the customer. The contract does not include any minimum purchase requirements, but it is highly likely that the customer will purchase parts from the supplier. Each part is distinct and is transferred to the customer at a point in time.

The nature of the promise in this example is the delivery of the parts rather than a service of standing ready to deliver. The contract provides a right to choose the quantity of additional distinct goods, in contrast with the preceding example's right to use the services for which control is being, or has been, transferred to the customer in the form of continuous access to the platform. In other words, the supplier is not obligated to transfer any parts until the customer submits a purchase order, while in the prior example, the transaction processor is obligated to make the platform (promised services) available to the customer without any additional decisions made by the customer.

It should be noted that not all transaction processing activities and MSAs should be accounted for as outlined in these examples. The determination of whether a contract contains variable consideration or an optional purchase depends upon the nature of the promise and the specific facts and circumstances of each situation.

Minimum purchase commitments

Often entities include a minimum purchase commitment, or a 'floor', within their contracts to ensure a minimum amount of revenue. Questions have arisen as to whether it is appropriate to recognise a portion of the revenue attributable to the floor ratably over the contract period.

Example 2 - Contracts with minimum purchase commitments (or 'floors')

Part 1: When an entity expects that the minimum purchase commitment will be met

A manufacturing entity executes a three-year MSA with a customer on 1 January 20X0, which allows it to be the exclusive provider of parts A, B, and C. The MSA specifies that the price for parts A, B, and C are CU 100, CU 150, and CU 200 respectively. The entity determines that the contract pricing is at the stand-alone selling prices of the individual products. The MSA also specifies a minimum purchase requirement of CU 30,000 over the three-year contract period. The customer will submit individual purchase orders specifying the quantity and mix of parts A, B, and C that it wishes to purchase throughout the three-year agreement. After the first purchase order is submitted, the entity concludes that it passes Step 1 of the revenue model and that each part is distinct. The entity transfers control of the parts to the customer at a point in time.

The manufacturing entity's sales under the MSA for the three-year period are as follows:

Year-end	Annual sales (CU)
31 December 20X0	8,000
31 December 20X1	15,000
31 December 20X2	10,000
Total	33,000

In determining how to account for the contract, the entity determines that the nature of its promise to the customer is the delivery of parts. The entity is not obligated to transfer any parts until the customer submits a purchase order specifying the quantity of parts A, B, and C it wishes to purchase. In other words, the contract contains an option to purchase additional goods, not variable consideration. Because the pricing for the additional parts is at the stand-alone selling price, the entity concludes that the contract does not contain a material right.

Analysis

Assuming the entity expects the customer to purchase at least the minimum amount of parts at all points throughout the contract, the entity recognises revenue of CU 8,000 in Year 1, CU 15,000 in Year 2, and CU 10,000 in Year 3 when control of the parts transfers to the customer. A customer's purchase under an MSA is not similar to a stand-ready obligation. When a customer submits a purchase order, it is contracting for a specific number of distinct goods, and the new purchase order creates new performance obligations for the supplier.

Assume the same facts in Part 1 above, except that the manufacturing entity's estimated sales under the MSA for the three-year period and actual sales (using hindsight) are as follows:

Year-end	Estimated total contract sales at beginning of reporting period (CU)	Annual sales (CU)
31 December 20X0	30,000	1,000
31 December 20X1	10,000	5,000
31 December 20X2	15,000	10,000
Total		16,000

In this case, while the entity expected the contractual minimum to be met in Year 1, and therefore does not recognise breakage in year one, after 31 December 20X0, the entity reevaluated its position and determined that it does not anticipate its transaction price to exceed the contractual minimum.

Example 2 – Contracts with minimum purchase commitments (or ‘floors’) (continued)

Part 2: When an entity expects that the minimum commitment will not be met and the floor is enforced

Analysis (continued)

We believe the entity may account for its expected obligations under this arrangement by applying a breakage model.

If applying the breakage approach, the entity would account for the expectation that the customer will order fewer than the minimum parts as breakage, and account for that breakage using the proportional method (whereby the entity recognises breakage revenue in proportion to the number of parts ordered) or the remote method (waiting to recognise breakage revenue until the likelihood that the customer will exercise its remaining rights becomes remote).

For this particular example, we do not believe the entity may apply the modification approach to account for its expectation that the customer will not meet its minimum purchase commitment, because the modification guidance applies only when the rights and obligations in the contract change (ie a change in price and/or scope). Because the contract stipulates no established minimums for each annual period, the customer does not decide to change its rights or obligations during the contract (eg after 31 December 20X0).

Reassessing variable consideration

An entity revises its estimate of variable consideration, including the application of the constraint, at the end of each reporting period to align with changes in facts and circumstances. Changes in estimates of variable consideration are accounted for in the same manner as other adjustments to the transaction price.

Estimating gross revenue as principal in arrangements involving a distributor

In some transactions involving a distributor, the supplier may not know the amount of the transaction price paid by the end customer to the distributor. In situations where the supplier concludes it is acting as a principal with respect to the underlying goods or services, but only knows the net amount it receives from the distributor, questions have arisen regarding the determination of the transaction price to be recorded by the supplier. Entities may consider estimating the transaction price following the guidance for variable consideration; however, in order to apply the guidance regarding variable consideration, the uncertainty in the transaction price must ultimately be resolved at some point in the future. If such uncertainty is not expected to ever be resolved, the amount charged by the distributor to the end customer is not considered variable consideration and would not be part of the transaction price.

Example 3 – Estimating gross revenue as a principal

Consider an example where Supplier A makes sales to an end customer through a distributor, and does not know the transaction price paid by the end customer to the distributor. Supplier A only knows the amount of the payment it receives from the distributor and never obtains access to the details of the transaction price paid by the end customer.

Analysis

In this situation, even if Supplier A concludes it is acting as a principal with respect to the equipment sold to the end customer, it would recognise revenue equal to the net amount it receives from the distributor. It would be inappropriate for Supplier A to estimate the transaction price paid by the end customer because the guidance regarding variable consideration does not apply when the uncertainty.

Significant financing components

In determining the transaction price, an entity reflects the time value of money if the agreed-upon timing of payments in the contract includes a significant financing component, whether explicit or implicit. The objective in adjusting the transaction price for the time value of money is to reflect revenue for the selling price as though the customer had paid cash for the goods or services when the entity transferred those goods or services. Either party may benefit from financing – ie the customer may pay before the entity performs its obligation (a customer loan to the entity) or the customer may pay after the entity performs its obligation (a loan by the entity to the customer).

To determine whether a contract contains a significant financing component, an entity considers all relevant facts and circumstances, including, but not limited to, the following:

- the difference, if any, between the promised consideration and the cash price that would be paid if the customer had paid as the goods or services were delivered, and
- the combined effect of the time between delivery of the goods or services and receipt of payment, as well as the prevailing market interest rates.

A contract with a customer would not have a significant financing component if any of the following factors exist:

- the customer paid for the goods or services in advance but the timing of the transfer of those goods or services is at the discretion of the customer
- a substantial amount of the consideration promised by the customer is variable and the amount or timing of that consideration varies on the basis of the occurrence or non-occurrence of a future event that is not substantially within the control of the customer or the entity, or
- the difference between the promised consideration and the cash price relates to something other than financing, and the difference between those amounts is proportional to the reason for the difference, such as protecting one of the parties from the other party's non-performance.

Practical insight – Financing component or not?

Description

Analysis

A customer pays in full at contract inception for the construction of a building expected to be completed 20 months from contract inception.

There appears to be a financing component because the customer pays 100% of the consideration more than 12 months before the entity completes part of its performance obligation (ie construction done in months 13-20). The entity needs to determine if the financing component is significant.

An entity constructs a building over three years. The customer makes quarterly progress payments and retains 10% of consideration due until construction is complete.

The difference between the promised consideration and the cash price relates to something other than financing (ie retention) and the entity considers the difference proportional to the reason for the difference. As a result, there does not appear to be a financing component in this contract.

An entity agrees to produce a large machine for a customer. The entity determines that control transfers when the customer takes possession of the machine. The payment terms specify that the customer must pay the entity 24 months after taking possession of the machine.

There appears to be a financing component because the customer makes payments more than 12 months after the entity's performance is complete. The entity needs to determine if the financing component is significant.

As a practical expedient, an entity need not adjust the promised amount of consideration for the effects of a significant financing component if the entity expects, at contract inception, that the period between when the entity transfers a promised good or service to a customer and when the customer pays for that good or service will be one year or less.

Practical insight – How should entities determine if the practical expedient can be applied when there is a single payment stream for multiple performance obligations?

At its March 2015 meeting, the TRG considered the following example:

An entity offers a 24-month contract to customers which includes the delivery of a device at contract inception and related services over 24 months. The entity concludes that the device and services are each distinct. The promised amount of consideration (combined amount for device and services) is CU 2,400, payable in 24 monthly installments of CU 100. Assume that the transaction price is allocated both to the device (CU 500) and to the services (CU 1,900 or CU 79 per month).

Assuming that the arrangement contains a significant financing component, the TRG discussed whether the practical expedient can be applied.

The TRG generally agreed that, absent evidence supporting which performance obligation a payment specifically relates to, an entity should proportionally allocate the consideration to the performance obligations in the contract for purposes of determining whether the practical expedient applies. For example, the contract terms may provide evidence supporting allocation of the payment to specific performance obligations.

Assume that the entity transfers the device first and recognises revenue for CU 500. Each month, the entity transfers the services and recognises revenue of CU 79 per month. Assuming that the cash payment cannot be directly tied to the device, the entity would proportionally allocate the monthly consideration to the device and services. Therefore, each month the entity would allocate CU 79 of the cash to the services and CU 21 to the device. The amount related to the service receivable is fully settled at the end of each month. However, because it will receive the full amount outstanding on the device over 24 months (CU 21 per month for 24 months), the entity concludes that the period between delivery of the device and receipt of the related consideration will be more than one year. Therefore, in this case, the practical expedient does not apply and the entity would adjust the transaction price for the time value of money.

Practical insight – If the promised consideration is equal to the cash selling price, does a financing component exist?

At its March 2015 meeting, the TRG considered the following example in paper 30 ‘Significant financing components’:

A furniture retailer offers a promotion for a CU 20,000 dining set. Customers have the option to obtain 0% financing for three years as part of this special promotion or to pay the entire amount at the time of purchase.

The TRG reached general agreement that an entity should not automatically assume that there is not a significant financing component when the list price, cash selling price, and the promised consideration are all equal. The difference, if any, between the amount of promised consideration and the cash selling price is one, but not the only, consideration in determining whether a significant financing component exists. The entity must consider all relevant facts and circumstances and apply judgement in determining whether a significant financing component exists in a contract. If the entity in the example offers a discount from list price to customers that pay in full upfront, this may indicate that the transaction includes a financing component.

However, if, on the other hand, the list price, cash selling price, and the promised consideration are in fact all equal, this may indicate that there is not a financing component (or if there is a financing component it is not significant).

Adjusting for a significant financing component

To adjust the amount of consideration for a significant financing component, the entity should use the discount rate applicable to a separate financing transaction between itself and the customer at contract inception. This rate must encapsulate the credit risk of the party receiving credit (for example the customer’s rate for deferred payments or the vendor’s rate for advance payments).



Example 4 - Determining the discount rate

An entity enters into a contract with a customer to sell equipment. Control of the equipment transfers to the customer when the contract is signed. The price stated in the contract is CU 3 million with a 6% contractual rate of interest, payable in three equal annual instalments of CU 1,122,329.

Analysis

Case A - Contractual discount rate reflects the rate in a separate financing transaction

In evaluating the discount rate in the contract that contains a significant financing component, the entity observes that the 6% contractual rate of interest reflects the rate that would be used in a separate financing transaction between the entity and its customer at contract inception (ie the contractual rate reflects the credit characteristics of the customer).

The market terms of the financing mean that the cash selling price of the equipment is CU 3 million. This amount is recognised as revenue and as a loan receivable when control of the equipment transfers to the customer.

Case B - Contractual discount rate does not reflect the rate in a separate financing transaction

In evaluating the discount rate in the contract that contains a significant financing component, the entity observes that the 6% contractual rate of interest is significantly lower than the 10% interest rate that would be used in a separate financing transaction between the entity and its customer at contract inception (ie the contractual rate does not reflect the credit characteristics of the customer). This suggests that the cash selling price is less than CU 3 million.

The entity determines the transaction price by adjusting the promised amount of consideration to reflect the contractual payments using the 10% interest rate that reflects the credit characteristics of the customer. Consequently, the entity determines that the transaction price is CU 2,791,067 (three annual payments of CU 1,122,329 discounted at 10%). The entity recognises revenue and a loan receivable for that amount. The entity accounts for the loan receivable in accordance with IFRS 9.

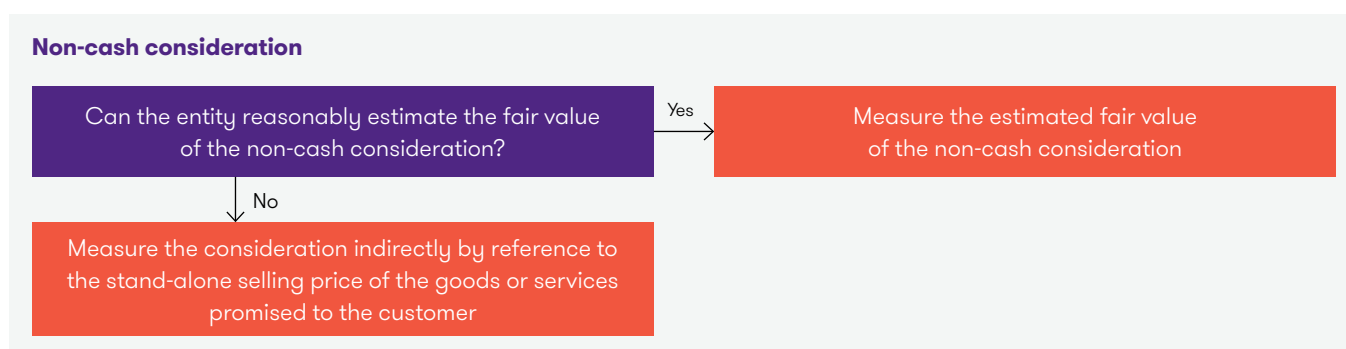
Presentation

The effects of financing, represented by interest revenue or interest expense, must be presented separately from revenue from contracts with customers in the statement of comprehensive income. Recognition of interest revenue or expense is contingent on the recognition of a contract asset (or receivable) or a contract liability in accounting for a contract with a customer.

Non-cash consideration

Sometimes a customer promises to pay for a good or service in a form other than cash, such as shares of common stock or other equity instruments, advertising, or equipment. An entity measures the estimated fair value of the non-cash consideration when determining the transaction price.

The starting point for estimating fair value is the non-cash consideration itself. However, if the entity cannot reasonably estimate the fair value of the non-cash consideration, the entity looks to the stand-alone selling price of the goods or services that it is providing to the customer in exchange for the consideration in accordance with the contract.



Non-cash consideration includes goods or services provided by the customer to the vendor if the vendor obtains control of those goods or services. Often, customer-supplied goods or services may be provided to the vendor, but the vendor does not obtain control. That said, a customer may transfer control of the goods or services to the vendor instead of cash to help the vendor fulfill its obligation under the contract. The following example demonstrates the accounting for tooling that is contributed by the customer for an entity to use in manufacturing customised parts for the customer. Common categories of tooling include molds, dies, and jigs.

Example 5 - Contributed goods or services

A manufacturing entity agrees to build five parts for a customer. The customer agrees to pay CU 100,000 for the parts and contributes tooling to be used in the entity's production process. The tooling has a fair value of CU 25,000 at contract inception.

Analysis

The entity determines that each part represents a single performance obligation and that control of the parts transfers to the customer upon delivery. It takes the entity approximately two months to build each part.

The entity takes ownership of the tooling, and can use the tooling for other projects and determines that it obtains control of the tooling in accordance with IFRS 15.

As a result, the entity includes the fair value of the contributed goods in the total transaction price, which it determines to be CU 125,000.

Date of measurement of non-cash consideration

IFRS 15 does not specify the date at which non-cash consideration should be measured. Consequently, management judgement will be required to determine the most appropriate single measurement date. For example, this could be:

- contract inception
- when the non-cash consideration is received, or
- at the earlier of when the non-cash consideration is received and when the related performance obligation is satisfied.

Subsequent measurement of non-cash consideration

If the fair value of non-cash consideration varies solely because of the form of the non-cash consideration (for example, due to changes in share price where consideration is paid in shares), the variable consideration constraint does not apply. The transaction price is not adjusted for subsequent changes in the fair value of consideration arising due to its form (for example changes in share price).

In contrast, if the fair value of non-cash consideration changes for reasons other than the form of the consideration (for example, the entity may receive an additional 100 shares if the entity's performance under the contract meets certain quality ratings), the entity is required to apply the guidance on variable consideration and the constraint when determining the transaction price, considering the performance bonus.

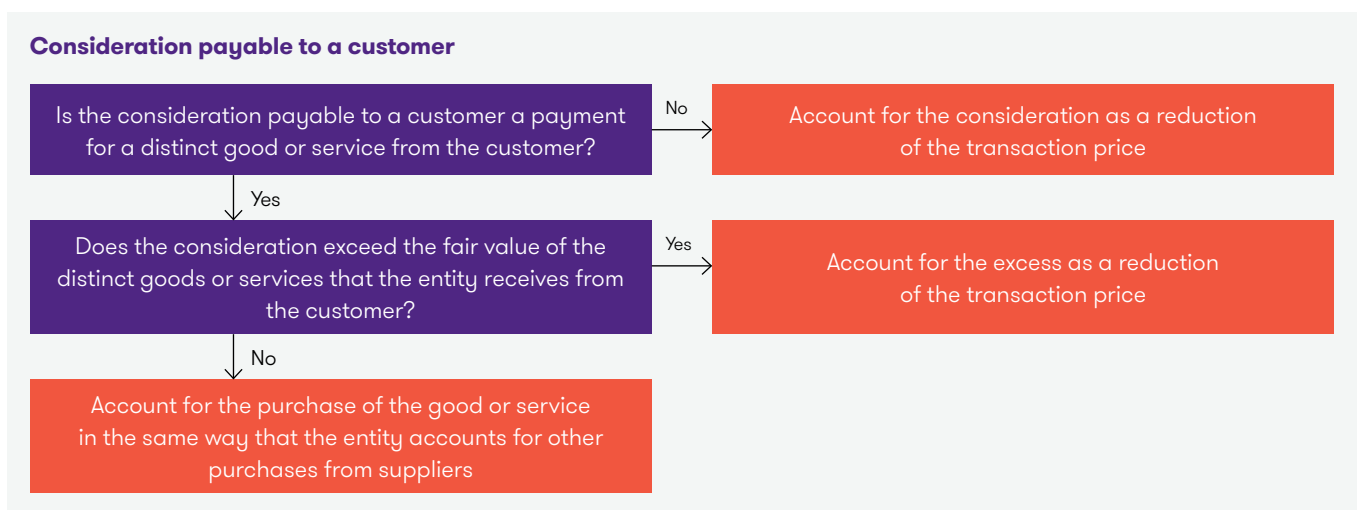


Consideration payable to a customer

Consideration payable to a customer includes amounts that an entity pays or expects to pay to a customer and occurs in many forms, including cash, credits, or other items that the customer can apply against amounts owed to the entity. Consideration payable to a customer may include, but is not limited to, the following:

- Slotting fees
- Cooperative advertising arrangements
- Pay-to-play payments
- Rebates or coupons

The key to appropriately accounting for consideration payable to a customer is determining whether the payment is made in exchange for a distinct good or service.



If, after applying the above guidance, an entity determines that the consideration it paid, or promises to pay, to a customer is a reduction of the transaction price, that reduction is recognised at the later of when the entity:

- recognises revenue for the goods or services, or
- pays or promises to pay the consideration.

Slotting fees (payments made by a supplier to a retailer for shelf space allocated to their products)

Example 6 – Consideration payable to a customer

A manufacturer of consumer goods enters into a one-year agreement with a major global retail chain. Under the contract, the customer commits to purchasing a minimum of CU 10 million worth of products over the year. At the start of the contract, the manufacturer makes a non-refundable payment of CU 1 million to the customer. This payment is intended to compensate the customer for modifications to its shelving systems required to accommodate the manufacturer's products.

Analysis

Upon evaluating the arrangement under IFRS 15, the manufacturer concludes that the payment is not in exchange for a distinct good or service, as it does not obtain control over the rights to the shelving. Therefore, the CU 1 million payment is treated as a reduction of the transaction price at the point revenue is recognised. As goods are delivered to the customer, the manufacturer reduces the transaction price proportionally – by 10% (CU 1 million ÷ CU 10 million).

For example, in the first month, the manufacturer invoices CU 1.5 million for goods delivered. It recognises revenue of CU 1.35 million, reflecting a CU 0.15 million reduction for the consideration payable to the customer.

Pay-to-play payments (payments to incentivise future business) and payments to reimburse the customer for the costs of switching suppliers

Practical insight – How should an entity account for an upfront payment when that payment relates to both current and anticipated contracts?

Consider the following example:

A supplier makes a CU 0.4 million payment to a potential new customer as part of its negotiations for a multi-year exclusive supply contract to provide specialised parts that are a component in the target customer's main product. The payment is made as an incentive and also to reimburse the customer for costs incurred to switch from its existing supplier, including termination fees and other costs. The payment is not in exchange for a distinct good or service. The target customer provides a nonbinding forecast of its supply requirements, with total expected future purchases under the exclusive supply agreement of CU 5 million.

How the supplier should account for the upfront payment will depend upon the particular facts and circumstances surrounding the upfront payment. Payments made to a customer may be recognised as either an asset or as an expense.

It would be unlikely for an entity to make a substantial payment to a customer without a valid expectation that the customer will enter into a future contract. Therefore, after considering the specific facts and circumstances surrounding the payment, the entity may conclude that the payment to the customer constitutes an asset, which would be amortised as a reduction in revenue as the expected goods are supplied to the customer. In such cases, the entity would need to evaluate the asset for impairment in subsequent periods. The impairment assessment should generally be evaluated on the basis of expected future revenue from the customer. Depending on the facts and circumstances of a particular situation, the entity may conclude, however, that the payment is best reflected as an expense when paid. This may be appropriate if an existing contract is not in place (for example, an entity makes a payment in anticipation that the customer will enter into a purchase contract) and the entity deems that the payment does not constitute an asset.

In determining whether an advance payment to a customer meets the definition of an asset, the supplier should consider the reason for the payment, and whether it is probable that the payment will be recoverable through future purchases by the customer. In assessing the probability of future purchases, relevant considerations could include whether the contract provides exclusivity, any minimum purchase terms, the expected margin, the nature and market position of the customer and their products, the life of the agreement, and any expected renewals.

The determination of whether the payment represents an asset or expense is not an accounting policy election. Instead, an entity should consider the facts and circumstances surrounding the payment, apply judgement, and make appropriate disclosures.

Cooperative advertising

An entity may agree to pay its customer certain amounts in exchange for the customer advertising the entity's products or services. In this case, the entity is required to evaluate the contract to determine if it receives a distinct good or service in exchange for the payment.

Example 7 – Cooperative advertising arrangements

An entity that manufactures sinks sells its products to a home goods retailer. The entity's contract with the retailer specifies that the entity will deliver 5,000 sinks for CU 1,000 per sink and will give the retailer a credit of CU 100,000 for advertising its products in the retailer's store circulars. The entity receives a copy of the retailer's circular, which evidences the advertising on its behalf, and concludes that the fair value of the advertising approximates CU 100,000.

Analysis

The entity evaluates the criteria in IFRS 15 to determine if the advertising is distinct. The entity concludes that the advertising is capable of being distinct. The entity concludes that the advertising is also distinct within the context of the contract because the advertising does not customise or modify the promise to transfer the sinks, and the sinks do not customise or modify the advertising. In addition, there is no significant integration service, and the advertising and sinks are not highly interdependent or highly interrelated since they do not significantly affect each other.

As a result, the entity accounts for the advertising payment as it does for other purchases of advertising services from suppliers (for example, in distribution expenses).

The fair value of the advertising is equal to the credit given to the customer, and therefore an advertising expense of CU 100,000 is recognised.

Variation:

If the fact pattern was the same as the example above, however, the advertising had a fair value of CU 80,000, then an advertising expense of CU 80,000 would be recognised. The CU 20,000 excess of the consideration payable to the customer over the fair value of the advertising would be treated as a reduction in transaction price.

How we can help

We hope you find the information in this article helpful in giving you insight into aspects of IFRS 15. If you would like to discuss any of the points raised, please speak to your usual Grant Thornton contact or visit www.grantthornton.global/locations to find your local member firm.



© 2026 Grant Thornton International Ltd. All rights reserved.

'Grant Thornton' refers to the brand under which the Grant Thornton member firms provide assurance, tax and advisory services to their clients and/or refers to one or more member firms, as the context requires. Grant Thornton International Ltd (GTIL) and the member firms are not a worldwide partnership. GTIL and each member firm is a separate legal entity. Services are delivered by the member firms. GTIL does not provide services to clients. GTIL and its member firms are not agents of, and do not obligate, one another and are not liable for one another's acts or omissions.