

# IFRS Adviser Alert

## Insights into IFRS 15 *Revenue from Contracts with Customers*

June 2026

### Executive summary

Grant Thornton International Ltd has published two new publications in the *Insights into IFRS 15* series:

- *Step 2: Identifying a performance obligation;*
- *Principal versus agent considerations.*

Revenue recognition is fundamental in all businesses, and it is important that it is recognized in a consistent and comparable way across industries and capital markets. IFRS 15 *Revenue from Contracts with Customers* was a result of the International Accounting Standards Board (IASB) and Financial Accounting Standards Board (FASB) joint project to improve the financial reporting of revenue under IFRS Accounting Standards and US GAAP. The standard makes it clear that its purpose is not to redefine the concept of revenue, but rather to ensure that revenue is consistently recognized at the appropriate time and at the most reliable amount.

The *Insights into IFRS 15* series summarizes the key areas of the standard, highlighting some areas that are challenging to apply in practice, to assist reporting entities in understanding how to apply IFRS 15's requirements.

The first new publication looks at step two of IFRS 15's five-step model, which covers the identification of performance obligations – the key units of account of IFRS 15. The second new publication covers whether a party to a contract is acting as a principal or as an agent. This can require applying significant judgement and will affect how revenue is recognized. The new publications are as follows:

- *Step 2: Identifying a performance obligation;*
- *Principal versus agent considerations.*



## Resources

The publications mentioned above follow this *IFRS Adviser Alert*.

## Follow us



[rcgt.com](http://rcgt.com)

### About Raymond Chabot Grant Thornton

Raymond Chabot Grant Thornton is a leading accounting and advisory firm providing audit, tax, and advisory services to private and public organizations. Together with Doane Grant Thornton in Canada, Raymond Chabot Grant Thornton has more than 5,650 people in offices across Canada. Raymond Chabot Grant Thornton is a member firm within Grant Thornton International Ltd. (Grant Thornton International). Grant Thornton International and the member firms are not a worldwide partnership. Services are delivered independently by the member firms.

We have made every effort to ensure the information in this publication is accurate as of its issue date. Nevertheless, information or views expressed herein are neither official statements of position nor should they be considered technical advice for you or your organization without consulting a professional business adviser. For more information about this publication, please contact your Raymond Chabot Grant Thornton adviser.

# Insights into IFRS 15

## Step 2: Identifying a performance obligation

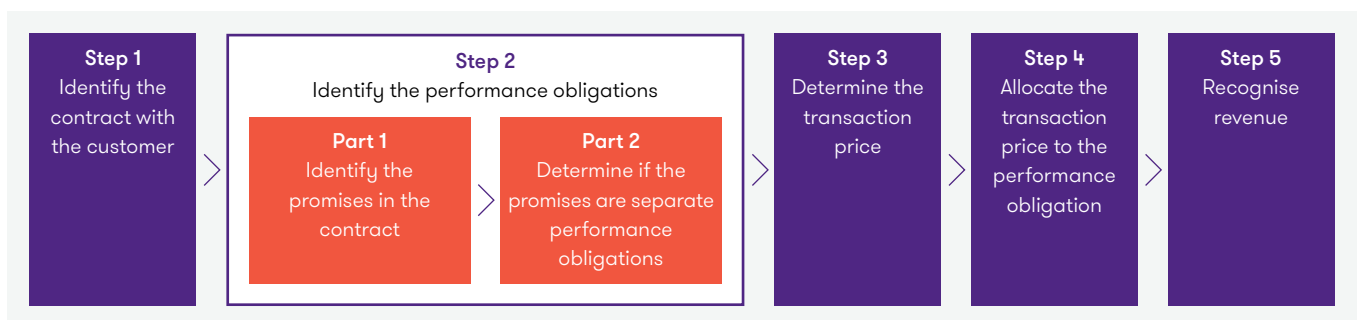


Accurate and consistent revenue recognition is a cornerstone of sound financial reporting for all businesses, ensuring comparability across industries and markets. IFRS 15 ‘Revenue from Contracts with Customers’ was jointly developed by the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) to align revenue reporting practices under IFRS and US GAAP. The objective of the standard is not to alter the definition of revenue, but to improve comparability by establishing a clear framework for recognising and measuring revenue.

Our ‘Insights into IFRS 15’ series summarises the key areas of the Standard, highlighting some areas that are challenging to apply in practice, to assist reporting entities in understanding how to apply IFRS 15’s requirements.

IFRS 15 introduced the five-step model for revenue recognition and applies specifically to contracts with customers. This article deals with Step 2 of the five-step model which covers the identification of performance obligations – the key units of account of IFRS 15. For a summary of the five-step model, refer to our article ‘[Insights into IFRS 15 – Overview and scope](#)’.

Step 2 is a two-part process. Before an entity can identify its performance obligations, it must first identify all the promised goods or services in the contract. Only after an entity identifies its promises can it then determine which of those promised goods or services constitute performance obligations.



# Identifying the promises in the contract

Promises are often explicitly specified in a contract but also may be implied by an entity's customary business practices, published policies, or specific statements that, at contract inception, create a reasonable expectation of the customer that the entity will transfer a good or service.

When identifying promises, an entity should consider the customer's perspective because contractual promises are part of the negotiated exchange between the entity and the customer. In addition, implied promises do not need to be enforceable by law. If a customer has a valid expectation that the entity has made a promise, the customer would view the promise as part of the contract. Some examples of promises in connection with customer contracts are listed below.

<b>Promise</b>	<b>Example</b>
<b>Sales of goods produced</b>	A manufacturing entity sells inventory
<b>Resale of goods purchased</b>	A retail entity sells purchased merchandise
<b>Resale of rights to goods or services purchased by an entity</b>	A hospitality entity that purchased a concert ticket resells the ticket, acting as principal
<b>Performing tasks</b>	A professional services entity provides consulting services
<b>Providing a service of standing ready to provide goods or services or of making goods or services available for a customer to use as and when the customer decides</b>	A manufacturing entity provides maintenance services on machines sold to a customer when the customer decides it wants the services performed
<b>Providing the service of arranging for another party to transfer goods or services</b>	A general maintenance entity acting as an agent provides a service of arranging for an unrelated party to provide specialised elevator maintenance to a customer
<b>Constructing, manufacturing, or developing an asset on behalf of a customer</b>	A contractor builds a hospital
<b>Granting licenses</b>	An entity grants a license to use its trade name
<b>Granting options to purchase additional goods or services that create a material right</b>	A retailer grants a customer an option to buy three items and to receive 60% off on a fourth item at a later date

## Administrative or pre-production services and activities

IFRS 15 defines 'promises' as those activities that transfer goods or services to the customer. In addition to the promised goods and services, an entity may be required to perform certain administrative or pre-production services or activities (for example in a contract that requires significant setup costs). If these do not transfer a good or service to a customer, they are not considered promises in a contract with a customer, regardless of whether a payment from the customer is received when those services are provided. If payment is received for services or activities that do not directly transfer a good or service to the customer, the payment should be accounted for as part of the transaction price, which is allocated to the identified performance obligations. Our article ['Insights into IFRS 15 – Determining the transaction price'](#) considers upfront payments in more detail.

## Inconsequential or perfunctory promises

There is no exemption in IFRS 15 from accounting for performance obligations that are considered to be perfunctory or inconsequential. Instead, in assessing promises in the contract and identifying performance obligations, an entity should consider both materiality and the overall objective of IFRS 15 to report useful information about the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer.

## Shipping and handling

In some cases, an entity performs shipping and handling activities in connection with a contract for its goods. If the shipping and handling activities are performed before the customer obtains control of the goods, then the shipping and handling activities are not a promised service to the customer. Rather, shipping and handling are activities to fulfill the entity's promise to transfer the goods.

In contrast, if shipping and handling activities are performed after the customer obtains control of the goods, these activities may be providing a service to the customer.

To assess whether shipping and handling activities performed after the customer obtains control of the goods are a separate performance obligation, the nature of the underlying promise is critical.

If the contract consists of providing the customer with goods at the customer's premises at a lump sum price, this may indicate that there is a single performance obligation and revenue should be recognised once the performance obligation is met (ie the goods are delivered to the location). However, if the scope of the contract is not only to supply the goods but to arrange for shipping services at the request of the customer and the price is negotiated separately, this may indicate that there are two performance obligations – one for the goods and other for the shipping services.

### Stand-ready promises

A stand-ready promise is one where an entity provides a service of 'standing ready' to provide goods and/or services, or it makes the goods or services available for a customer to use as and when the customer decides.

#### Practical insight - What is the nature of the promise in a stand-ready obligation?

Entities will need to exercise judgement to determine whether the nature of the entity's promise is to stand ready to provide goods or services or to actually provide the underlying specified goods or services, which would not be a stand-ready obligation. An indicator as to the nature of the entity's promise might be when the entity's obligation is to provide a defined good or service, which would indicate that the nature of the entity's promise is to provide those underlying specified goods or services. If instead the entity determines that the nature of its obligation is to provide an unknown type or quantity of goods or services, this indicates that the nature of the entity's promise is to stand ready.

Judgement is necessary to determine when a promise is to stand-ready, as many contracts call for the entity to be prepared to provide the goods or services at the discretion of the customer, but not all such promises would necessarily lead to stand-ready performance obligations.



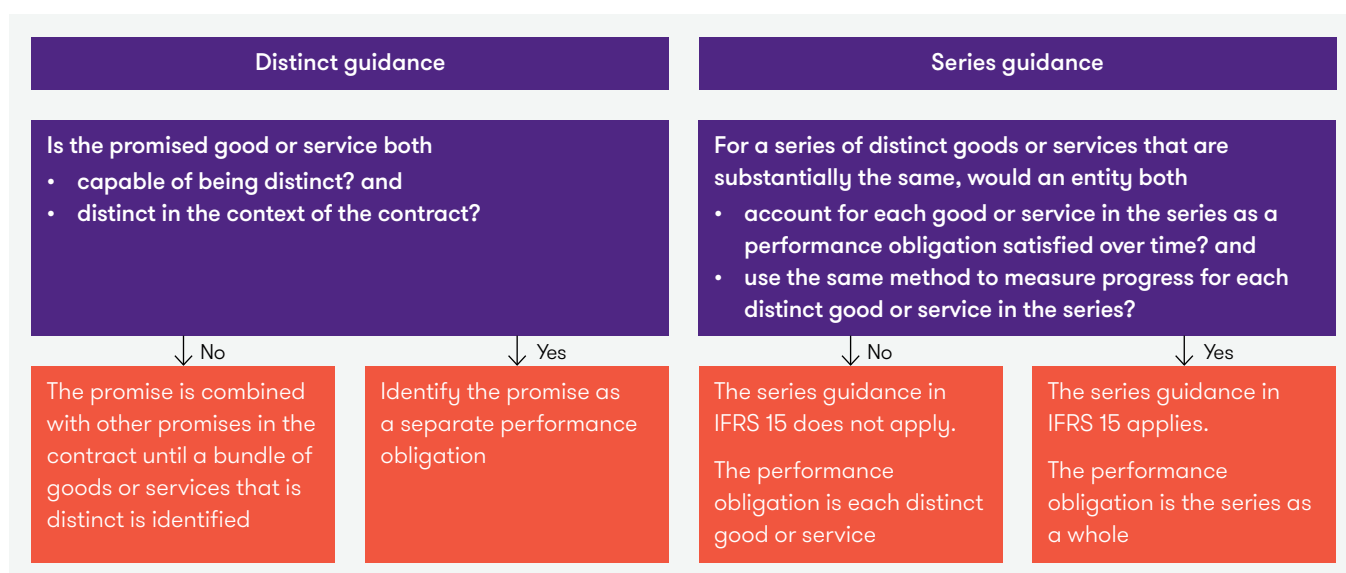
# Identifying performance obligations

After identifying the implicit and explicit promises in the contract, the entity must evaluate each promise to determine if that promise constitutes a performance obligation. This evaluation is performed at contract inception.

A performance obligation is a promise in a contract with a customer to transfer to the customer either:

- a good or service (or a bundle of goods or services) that is distinct, or
- a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.

Accordingly, an entity accounts for a promise as a separate performance obligation if the promise meets the criteria to be distinct or if it represents a series of distinct goods or services. This is illustrated in the following flowchart:



## Capable of being distinct

The first criterion for being 'distinct' is that the customer can benefit from the good or service either on its own or together with other resources that are readily available (that is, the good or service is capable of being distinct).

A customer can benefit from a good or service on its own if the good or service can be used, consumed, sold for an amount greater than scrap value, or otherwise held in a way that generates economic benefits.

Sometimes, a customer can benefit from a good or service only with other readily available resources. A 'readily available resource' is a good or service that is sold separately (by the entity or by another entity) or one that the customer has already obtained from the entity or from other events or transactions.

The fact that the entity regularly sells a good or service on its own is an indicator that the good or service is capable of being distinct.

The assessment of whether the customer can benefit from a good or service on its own should be based on the characteristics of the goods or services themselves, excluding contractual limitations that might preclude the customer from obtaining readily available resources from a source other than the entity. For example, if a contract states that a customer can purchase a specific good or service only from the entity, that would be irrelevant in determining if the customer can benefit from the goods or services on their own.

### Distinct within the context of the contract

In some situations, separately accounting for each promised good or service that is capable of being distinct would not faithfully represent the entity's performance in the contract. For instance, construction and production contracts often involve delivering a range of goods and services to the customer – such as building materials, labour, and project management – that are individually capable of being distinct. However, treating each of these components as separate performance obligations would lead to revenue being recognised when the materials and other inputs were supplied, rather than when the entity actually uses those inputs to carry out the construction or production activities. This would not reflect the substance of the entity's promise to the customer or the entity's performance.

As a result, a second criterion must also be met in order to conclude that a good or service is distinct and is therefore a performance obligation to be accounted for separately.

The second criterion for being 'distinct' is that the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract – that is, the promise to transfer the good or service is distinct within the context of the contract.

In assessing whether an entity's promise to transfer a good or service to the customer is distinct within the context of the contract, the objective is to determine whether the nature of the contractual promise is to transfer each of the goods or services individually or instead to transfer a combined item to which the promised goods or services are inputs. Significant judgement may be required to determine whether promised goods or services are distinct within the context of the contract.

IFRS 15 provides factors that indicate that a promise to transfer goods or services is not separately identifiable from other goods or services in the contract, and these are as follows:

- The entity provides a significant service of integrating the goods or services with other goods or services promised in the contract into a bundle of goods or services. In other words, the entity is using the goods or services as inputs to create a combined output specified by the customer.
- One or more of the goods or services significantly modifies or customises one or more of the other goods or services promised in the contract.
- The goods or services are highly interdependent or highly interrelated. In other words, the entity must evaluate whether each of the promised goods or services is significantly affected by one or more of the other goods or services in the contract. For example, in some cases, two or more goods or services are significantly affected by each other because the entity would not be able to fulfill its promise by transferring each of the goods or services independently.

Given the wide variety of revenue arrangements that are within the scope of IFRS 15, there may be instances where the factors will be less relevant to the evaluation of the separately identifiable principle. The list of indicators in IFRS 15 is explicitly not exhaustive so entities should consider the objective of the principle, in addition to the indicators provided when performing this assessment.



### Example 1 – Distinct goods and services

A manufacturing entity sells its customer a product. The contract also provides the customer with the right to receive up to 20 hours of training services on how to operate the product at no additional cost.

The entity assesses the goods and services in the contract to determine whether they are distinct and therefore give rise to separate performance obligations.

#### Analysis

The product is distinct because it meets both of the criteria in IFRS 15. The product is capable of being distinct because the customer can benefit from the product on its own without the training services. The entity regularly sells the product separately without the training services (as the training services, for instance, can be provided/supported by other participants in the market). In addition, the product is distinct within the context of the contract, because the entity’s promise to transfer the product is separately identifiable from other promises in the contract.

In addition, the training services are distinct because they meet both of the criteria in IFRS 15. The training services are capable of being distinct, because the customer can benefit from the training services on its own or together with the product that has already been provided by the entity. In addition, the training services are distinct within the context of the contract, because the entity’s promise to transfer the training services is separately identifiable from other promises in the contract. The entity does not provide a significant service of integrating the training services with the product. The training services are not significantly modified or customised by the product. The training services are not highly dependent on, or highly interrelated with, the product.

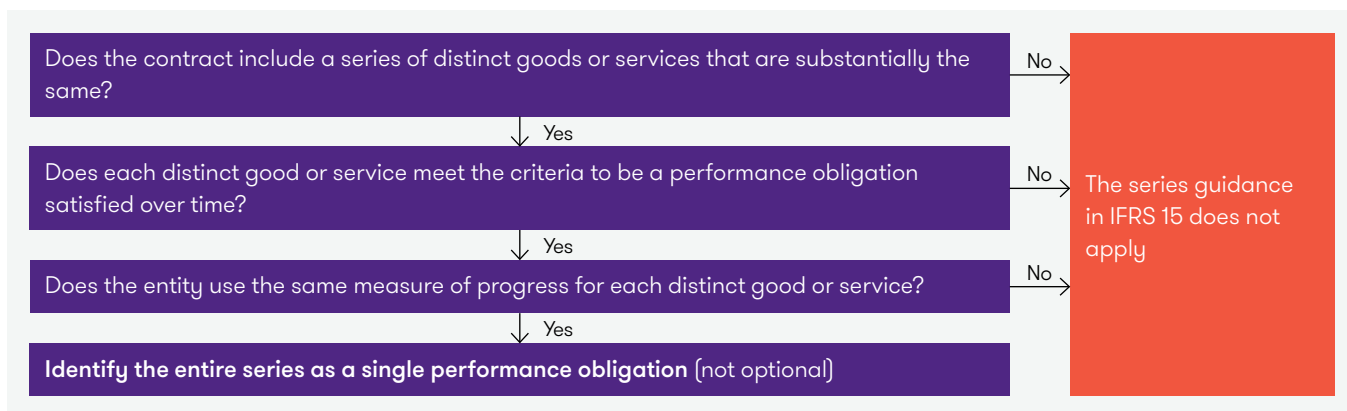
The product and training services are each distinct and therefore give rise to two separate performance obligations.

As a result, the entity allocates the transaction price to the two performance obligations (the product and the training services) and recognises revenue when (or as) those performance obligations are satisfied.

### Series of distinct goods or services

When an entity provides the same distinct goods or services over a period of time (for example, a repetitive service contract for cleaning), it needs to consider if the promised goods or services in the contract meet the requirements of the ‘series guidance’. Under the series guidance, an entity is required to account for a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer as a single performance obligation. The guidance is not optional, which means that an entity is required to account for the series as a single performance obligation rather than accounting for the goods or services as individual performance obligations if the criteria in IFRS 15 are met.

The following flowchart explains how to apply the series guidance:



### **Practical insight – What are some examples of goods or services that constitute a series?**

There are various examples of services that constitute a series, including the following:

- an entity provides weekly cleaning services to a customer for three years
- a hotel manager provides hotel management services to a customer for 20 years
- an entity provides monthly payroll processing services to a customer for one year
- an entity provides asset management services to a client for five years

Even though each instance of service (that is, each hour or day of service) is distinct, the entity accounts for each of these contracts as a single performance obligation because the entity transfers a series of distinct services that are substantially the same and that have the same pattern of transfer to the customer in each case. In other words, each service meets the over time criteria in IFRS 15 and the entity uses the same method to measure its progress (ie a time-based measure) in each case.

Other goods or services that might constitute a series include, but are not limited to, the following examples:

- a software as a service (SaaS) company providing a customer with continuous access to its platform
- a telecommunications company providing network access to customers over a period of time

### **Practical insight – How should an entity consider whether the performance obligation consists of distinct goods or services that are ‘substantially the same’?**

An entity first determines the nature of its promise in providing the service to the customer. If the nature of the entity’s promise is to deliver a specified quantity of a service, the entity should evaluate whether each service is distinct and substantially the same. If the nature of the entity’s promise is the act of standing ready or providing a single service for a period of time, the entity may consider whether each time increment (for example, each day or hour), rather than the underlying activity, is distinct and substantially the same. A series could consist of either distinct time increments or the good or service delivered, depending on the nature of the promise.

For example, an entity enters into a contract to provide monthly payroll processing services to a customer for one year. The nature of the entity’s promise is to deliver a specified quantity of a service – 12 distinct instances of payroll processing. It is not a promise to stand ready to perform an undefined number of processing tasks. As a result, the entity evaluates whether each instance of payroll processing is distinct and substantially the same.

In contrast, a hotel manager enters into a contract with a customer to manage a customer-owned property for 20 years. The hotel management service comprises various activities that may vary by day (for example, cleaning service, reservation services, and property maintenance). In this contract, the nature of the promise is the act of standing ready to provide the hotel management service each day because the entity has promised to provide an unspecified quantity of activities rather than a defined number of services. Accordingly, the entity considers whether each time increment is distinct and substantially the same.

### **Practical insight – In order to apply the series guidance, must the goods be delivered or services be performed consecutively?**

In order to apply the series guidance, the entity need not deliver the goods nor perform the services consecutively. In other words, the guidance still applies when there is a gap in delivery or service, provided the other criteria are met.

For example, an entity has contracted with a customer to provide a manufacturing service in which it will produce 24,000 units over a two-year period. The entity does not plan to perform evenly over the two-year service period. To meet the production targets, the entity produces 2,000 units in some months and zero units in other months. That is, the entity does not produce 1,000 units a month, continuously. Instead, the entity plans to perform the manufacturing service over the two-year period.

The units produced under this service arrangement are substantially the same and are manufactured to the specifications of the customer. The entity does not incur significant up-front costs to develop the production process. Assume that its service of producing each unit is a distinct service in accordance with the criteria in IFRS 15. Additionally, the service is accounted for as a performance obligation satisfied over time because the units are manufactured specific to the customer (such that the entity’s performance does not create an asset with an alternative use to the entity), and if the contract were to be cancelled, the entity has an enforceable right to payment (cost plus a reasonable profit margin).

Although the services are not performed consecutively, the criteria for applying the series guidance are met, and therefore the services are accounted for as a single performance obligation in accordance with the series guidance in IFRS 15.

## Customer options for additional goods and services

An entity that sells goods or services may also provide customers with an option to acquire additional goods or services for free or at a discount, for example, sales incentives, award credits or points, and renewal options. Under IFRS 15, an entity must identify the option as a separate performance obligation if the option represents a 'material right' to the customer that the customer would not have received without entering into that contract. If the option does not provide the customer with a material right (eg if the option only allows the customer to buy additional goods or services at their stand-alone selling price), the option is considered a marketing offer which does not result in a separate performance obligation.

When an entity determines that an option provides the customer with a material right, it identifies that option, not the underlying goods and/or services, as a separate performance obligation. In other words, when an entity determines that an option provides the customer with a material right, it will estimate the stand-alone selling price of the option and allocate a portion of the overall transaction price (excluding the amount a customer would pay for purchasing the additional goods or services) to the option. Our article '[Insights into IFRS 15 – Allocating the transaction price to the performance obligation](#)' discusses estimating the stand-alone selling price of an option.

### Example 2 – An option that provides the customer with a material right

An entity enters into a contract for the sale of Product A for CU 100. As part of the contract, the entity gives the customer a 40% discount voucher for any future purchases up to CU 100 in the next 30 days. The entity intends to offer a 10% discount on all sales during the next 30 days as part of a seasonal promotion. The 10% discount cannot be used in addition to the 40% discount voucher.

#### Analysis

Because all customers will receive a 10% discount on purchases during the next 30 days, the only discount that provides the customer with a material right is the discount that is incremental to that 10% (ie the additional 30% discount). The entity accounts for the promise to provide the incremental discount as a performance obligation in the contract for the sale of Product A.

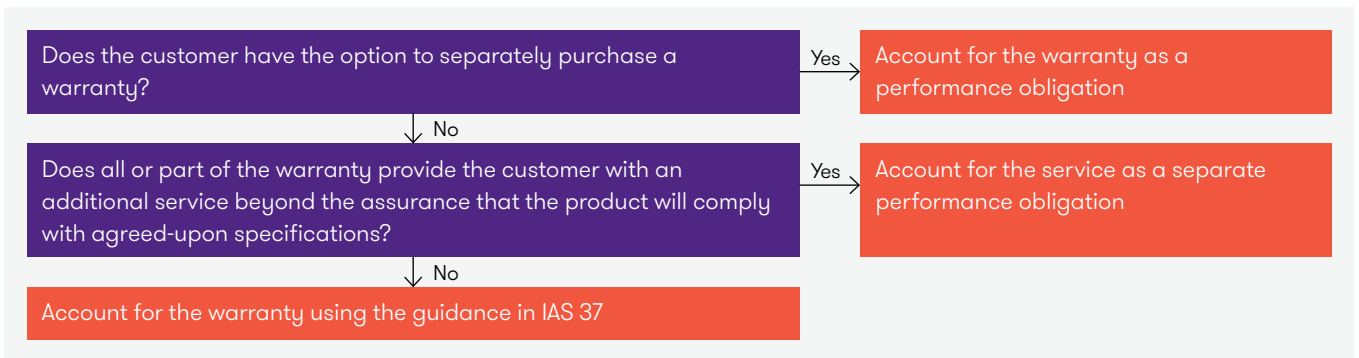
IFRS 15 does not contain explicit guidance on how an entity should account for a customer's exercise of a material right; however, the exercise of an option should not be accounted for as variable consideration. Instead, the Standard seems to support two reasonable approaches:

Approach	Insight article
<a href="#">Account for the exercise of the option as a continuation of the existing contract (ie by updating the transaction price)</a>	<a href="#">‘Insights into IFRS 15 – Determining the transaction price’</a>
<a href="#">Account for the exercise of the option as a contract modification</a>	<a href="#">‘Insights into IFRS 15 – Contract modifications’</a>

## Warranties

IFRS 15 contains guidance for the accounting for warranties provided to customers in connection with the sale of a good or service. If a customer has the option to separately purchase a warranty, then an entity accounts for that warranty as a separate performance obligation. If a customer does not have the option to separately purchase a warranty, then the entity accounts for the warranty using the guidance on product warranties in IAS 37 'Provisions, Contingent Liabilities and Contingent Assets', unless all or part of the warranty provides the customer with an 'additional service' beyond the assurance that the product complies with agreed-upon specifications.

The following flowchart explains how to account for warranties:



IFRS 15 lists the following factors that an entity should consider in determining whether a warranty provides a customer with an ‘additional service’.

Factor	Description
<b>Whether the warranty is required by law</b>	A legal requirement to provide a warranty indicates that the warranty is intended to protect the customer from purchasing a defective product.
<b>Term of the warranty coverage period</b>	The longer the coverage period, the more likely it is that the promised warranty includes a performance obligation because it is more likely to provide a service in addition to the assurance that the product complies with agreed-upon specifications.
<b>The nature of the tasks the entity promises to perform under the warranty</b>	If an entity needs to perform certain tasks to provide assurance to the customer that the product complies with agreed-upon specifications, those services would not likely constitute a separate performance obligation.



### Example 3 – Assurance type warranty

A manufacturing entity provides its customer with a warranty when purchasing a product. The warranty provides assurance that the product complies with agreed-upon specifications and will operate as promised for one year from the date of purchase. The warranty is not required by law, and the customer does not have an option to separately purchase the warranty.

The entity assesses whether the warranty gives rise to a separate performance obligation.

#### Analysis

The entity assesses the promise to provide a warranty and observes that the warranty gives the customer the assurance that the product will function as intended for one year. This is less than the expected life of the product. The services to be provided do not go beyond the promise that the product complies with agreed-upon specifications. Therefore, the entity concludes that the warranty does not provide the customer with a good or service in addition to that assurance and, therefore, the entity does not account for it as a separate performance obligation.

As a result, the entity allocates the transaction price to the single performance obligation (the product) and recognises revenue when (or as) that performance obligation is satisfied.

### Example 4 – Lifetime warranties

A luggage company provides a lifetime warranty that states “If your baggage is broken or damaged, we will repair it for free.”

Factor	Analysis
<b>Whether the warranty is required by law</b>	This indicator states that if the entity is required by law to provide a warranty, the existence of that law indicates that the promised warranty is not a separate performance obligation. In this example, because there is no law that requires the entity to make a promise for the lifetime of the product, this indicator suggests the warranty is, in fact, a performance obligation.
<b>Term of the warranty coverage period</b>	This indicator states that a longer warranty coverage period increases the likelihood that the warranty is a performance obligation. In this example, the length of the warranty is for the life of the baggage, so this indicator suggests that the warranty is a performance obligation.
<b>The nature of the tasks the entity promises to perform under the warranty</b>	In this example, the nature of the tasks not only includes repairing baggage that does not meet the promised specifications, but also includes replacing broken or damaged baggage for free. Because the baggage warranty goes beyond the promise that the baggage complies with agreed-upon specifications, this indicator suggests the warranty is a performance obligation.

#### Conclusion

The warranty provided by the baggage company constitutes an additional service, beyond the assurance that the product complies with agreed-upon specifications. Consequently, the additional service should be accounted for as a separate performance obligation.

Warranties that are not sold separately by the entity or negotiated separately with the customer should also be identified as performance obligations if the facts and circumstances suggest that the warranty (or a part of the warranty) provides a service to the customer in addition to the assurance that the entity's past performance was as specified in the contract. This provides a clear principle that allows an entity to account for economically similar warranties in a similar manner, regardless of whether the warranties are separately priced or negotiated.

The Standard clarifies that the following situations do not give rise to a performance obligation:

- a law that requires the entity to compensate the customer for harm or damage caused by its products when used by the customer for its intended purpose
- an entity's promise to indemnify the customer for liabilities and damages arising from claims of patent, copyright, trademark, or other infringement by the entity's products

An entity accounts for such obligations in accordance with the guidance on loss contingencies in IAS 37.

Some warranties may include both assurance features and service features. If an entity cannot reasonably account for those assurance features of the warranty separately from the service features, the entity should be allowed to account for the warranties together as a single performance obligation. This ensures that the entity does not overstate the recognition of revenue at the time that the product transfers to the customer and also relieves the entity from identifying and accounting separately for the two components of the warranty coverage.

## 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](http://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.

# Insights into IFRS 15

## Principal versus agent considerations



Revenue recognition is a key principle in financial reporting, underpinning the integrity and comparability of financial statements across industries and global markets. IFRS 15 ‘Revenue from Contracts with Customers’ was jointly developed by the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) to harmonise revenue reporting under IFRS and US GAAP. Rather than redefining what constitutes revenue, the Standard focuses on establishing a consistent framework for recognising revenue at the correct point in time and at a reliable amount. The Standard provides comprehensive guidance on accounting for revenue recognition – however, the detailed requirements of IFRS 15 can still be challenging for preparers of financial statements to apply.

Our ‘Insights into IFRS 15’ series summarises the key areas of the Standard, highlighting some areas that are challenging to apply in practice, to assist reporting entities in understanding how to apply IFRS 15’s requirements.

In many revenue transactions, more than one party is involved in delivering the goods and services to the customer. In those situations, it is sometimes difficult for an entity to determine whether it is acting as a principal or as an agent, and an entity must often apply significant judgement to reach a conclusion. While the principal-agent guidance in IFRS 15 does not eliminate the need for judgement, it is intended to make the principal versus agent assessment easier.

IFRS 15 requires an entity to determine whether the nature of its promise is to provide the specified goods or services to the customer or to arrange for another party to provide the goods or services to the customer. If the nature of the promise is to provide the specified goods or services directly to the customer, the entity is a principal and recognises revenue on a gross basis at the amount of consideration to which it expects to be entitled. In contrast, if the nature of the promise is to arrange for another party to provide the goods or services to the customer, the entity is an agent and recognises revenue in the net amount of the fee or commission it is entitled to for its agency services. In this case, the net amount might be the amount of consideration that the entity retains after paying the other party if the entity is responsible for collecting the full amount of consideration.

IFRS 15 establishes a two-step approach to assessing a principal-agent relationship in cases where a third party is involved in providing the goods or services to the customer. The entity first identifies the specified good or service to be provided to the customer. It then assesses whether it has control over the affected goods or services before they are transferred to the customer.

Under IFRS 15, ‘control’ of an asset refers to the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. Control includes the ability to prevent other entities from directing the use of, and obtaining the benefits from, an asset. The benefits of an asset are the potential cash flows (either inflows or savings in outflows) that might be obtained by using the asset to produce goods or provide services, to enhance the value of other assets, or to settle liabilities or reduce expenses:

- by selling or exchanging the asset
- by pledging the asset to secure a loan, or
- by holding the asset.

The following flowchart demonstrates how any entity should consider whether they are acting as a principal or as an agent:



### Identifying the specified goods or services promised to the customer

An entity determines whether it is a principal or an agent for each specified good or service promised to the customer. A specified good or service is a ‘distinct’ good or service or a ‘distinct’ bundle of goods or services to be provided to the customer. IFRS 15 defines ‘distinct’ goods and services as those that are both capable of being distinct and are separately identifiable from other promises in the contract (see our article ‘[Insights into IFRS 15 – Step 2: Identifying a performance obligation](#)’). If a contract contains more than one specified good or service, an entity should determine if it is principal or agent for each one and may be a principal for some goods or services and an agent for others.

#### Practical insight – Specified good or service – not performance obligation

The IASB decided to use the term ‘specified good or service’ rather than ‘performance obligation’ to describe the unit of account for purposes of the principal versus agent evaluation because using the term ‘performance obligation’ would have been confusing when the entity is acting as an agent. An agent’s promise (its performance obligation) is to arrange for another party to provide that party’s goods or services to the customer. In that circumstance, the specified good or service itself is not the agent’s performance obligation.

While the identification of the specified good or service may be straightforward in many contracts, it may be more difficult when an entity attempts to determine whether the specified good or service promised to the customer is the underlying good or service itself or whether it is a right to that good or service.

### Example 1 – Promise to provide goods or services (entity is a principal)

An entity enters into a contract with a customer to deliver office maintenance services. Both parties agree on the scope of the services and negotiate the pricing. The entity is responsible for ensuring the services are carried out in accordance with the contract terms. It invoices the customer monthly for the agreed amount, with payment due within 10 days of invoicing.

To deliver these services, the entity frequently engages third-party providers. Upon securing a contract with a customer, the entity contracts with a service provider to perform the office maintenance services for the customer. The payment terms with these providers generally align with those in the entity's customer contracts. However, the entity remains liable to pay the service provider even if the customer fails to pay.

#### Analysis

To assess whether the entity acts as a principal or an agent, it must identify the specific good or service promised to the customer and determine whether it controls that good or service before it is transferred.

In this case, the promised service is office maintenance. Although the entity acquires the right to these services from a third-party provider after entering into the contract with customer, that right is not transferred to the customer. The entity retains the ability to direct the use of, and obtain substantially all the remaining benefits from, that right, ie control over how and where the services are used. For example, it can choose to allocate the service provider to this customer, another customer, or even for its own use. The customer cannot instruct the service provider to perform services beyond what the entity has agreed to deliver.

Therefore, the right to office maintenance services obtained from the service provider is not the specified good or service in the customer contract.

(The analysis of this example continues in the section below on **evaluation of control**).

### Example 2 – Identifying the specified good or service when a third party is legally required to provide certain services in the contract

A wellness company provides cancer patients with an overall specified service of a 'cancer treatment and wellness program'. The wellness company developed its proprietary wellness program that caters to all of a cancer patient's needs throughout their cancer treatment and recovery journey. After completing a comprehensive intake form using the entity's proprietary approach, each patient is assigned a 'wellness leader', who customises the program for each patient, including program execution, chemotherapy treatments, physical and mental rehabilitation, and pharmacy needs. The chemotherapy treatments and physical rehabilitation are provided by licensed physicians, and the mental rehabilitation is performed by licensed psychologists, all vetted and engaged separately by the wellness company.

#### Analysis

The wellness company concludes that the specified good or service in the arrangement is its cancer treatment and wellness program. It determines that it is primarily responsible for providing this service to its customers and therefore is acting as the principal in the arrangement.

When considering the role of the licensed physicians and psychologists, the wellness company observes that it obtains control of the services provided by these doctors through its contractual relationships, and that it then directs the doctors to treat the patients on its behalf. Further, the wellness company notes that it integrates the individual services into a unique and comprehensive proprietary wellness program for each of its customers.

## Evaluating control

Once an entity has identified the specified goods or services to be provided to the customer, it must evaluate whether it controls those goods or services before they are transferred to the customer, in which case, it is acting as a principal in the transaction.

An important aspect of the guidance is that a principal either provides the specified good or service to the customer or engages another party to provide some or all of the good or service on its behalf.

### Obtaining control as a principal

In a transaction with more than one party providing goods or services to the customer, a principal obtains control of any one of the following prior to its transfer to a customer:

- a good or asset from the other party
- a right to service to be performed by the other party (ie the entity directs the other party on providing the service to the customer on its behalf), or
- a good or service from the other party that it then combines with other goods or services to provide the specified good or service to the customer.

The first instance is generally straightforward to identify. For example, a car dealer purchases 10 vehicles from a used-car auction for resale to third-party customers. The car dealer assumes inventory risk for the 10 vehicles while they are in its possession before the resale to the customers.

The second case may be less straightforward to identify. For example, as discussed in Example 1 above, an entity may engage a third-party service provider to provide office maintenance services to the entity's customers. The entity first obtains a contract with a customer and then enters into another contract with a service provider, directing the service provider to perform office maintenance services for the customer. The specified service is the office maintenance services. While the entity obtains a right to office maintenance services from the service provider after entering into the contract with the customer, that right is not transferred to the customer. In other words, the entity retains the ability to direct the use of, and obtain substantially all the remaining benefits from, that right.

An entity is also a principal when it obtains control of the third-party's good or service before it integrates the good or service with other goods or services that it provides to the customer as part of transferring control of the overall performance obligation. This situation is common in the engineering and construction industry where entities often engage third-party entities to perform pieces of an overall project (for example, to construct a building), but the entity retains overall responsibility for integrating all of the services into the combined output requested by the customer. The entity identifies a single performance obligation because it conducts a significant service by integrating the promises into the overall output for the customer. As a result, the entity would likely conclude that it is acting as principal.

### Example 1 – Promise to provide goods or services (entity is a principal)

#### Analysis (continued)

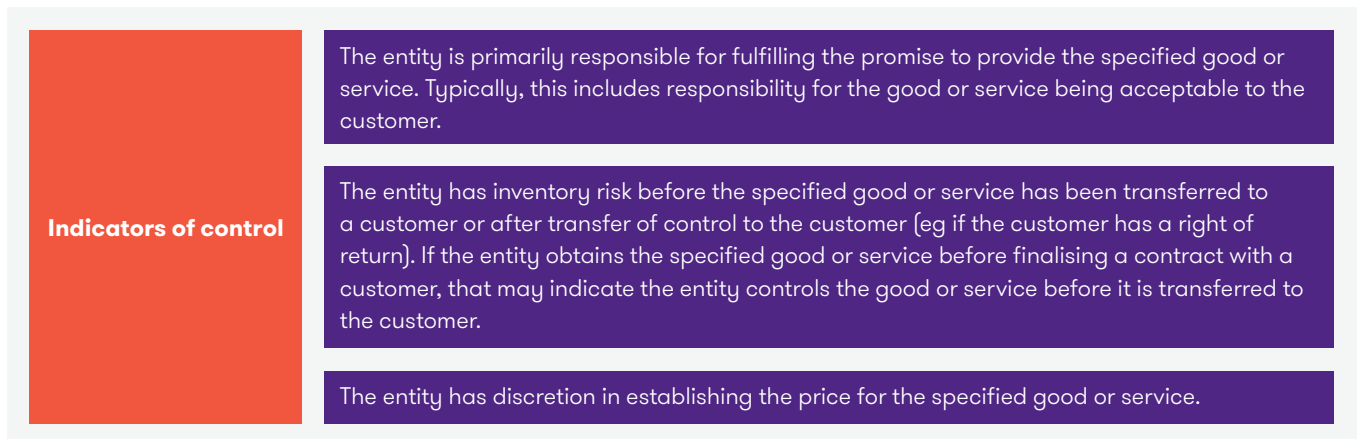
The entity concludes that it controls the specified services before they are provided to the customer. The entity obtains control of the right to office maintenance services after entering into the contract with the customer but before those services are provided to the customer. The terms of the entity's contract with the service provider give the entity the ability to direct the service provider to provide the specified services on the entity's behalf.

## Indicators of control

As set out in IFRS 15, the main criterion for assessing whether an entity is acting as principal or agent is the **existence or non-existence of control of the transferred goods or services by the reporting entity prior to the customer transaction**. To support the assessment of whether the entity obtains control of a good or service in situations where the assessment might be difficult, IFRS 15 includes three indicators that generally indicate a principal position in a customer transaction.

These indicators can have different weight depending on the type of goods or services involved and are also not to be understood as an exhaustive list. All relevant facts and circumstances are to be included in the assessment of control.

The below chart sets out these three indicators that an entity is principal:



Primary responsibility for fulfilling the promise to provide the specified good or service typically includes responsibility for the acceptability of the good or service. The assessment should also include whether the entity is directly responsible for delivering goods or services to the customer and who the customer considers to be primarily responsible for providing the service.

Inventory risk within the context of IFRS 15 can be presumed for the reporting entity if it is responsible for the proper condition of the goods at the time of their transfer to the customer, has committed to a specified minimum purchase quantity from its suppliers before the goods are purchased by the customer, and does not have a right of return to the supplier for goods not transferred to the customer.

Pricing discretion may be less relevant to the assessment of control if, for example, the market for the product means that the entity, in effect, has limited flexibility in setting prices.

The IASB included these indicators to support an entity's assessment of whether it controls the specified good or service before it is transferred or provided to the customer. It is important to emphasise that the indicators

- do not override the assessment of control
- should not be viewed in isolation
- do not constitute a separate or additional evaluation, and
- are not a checklist of criteria to be met in all situations or factors to be considered, in all scenarios.

Considering one or more of the indicators will often be helpful and, depending on the facts and circumstances, individual indicators will be more or less relevant or persuasive to the assessment of control.

### Practical insight - Indicators of control

The nature of the entity's promise may not always be readily apparent. For that reason, the IASB included indicators in IFRS 15 to help an entity determine whether the entity controls the goods or services before transferring them and thus whether the entity is a principal or an agent. Those indicators are based on indicators that were included in previous revenue recognition requirements. However, the indicators in IFRS 15 have a different purpose than previous revenue recognition requirements in that they are based on the concepts of identifying performance obligations and the transfer of control of goods or services.

### Practical insight - Indicators are not weighted

When an entity has an arrangement to provide goods and services to a customer that includes more than one party, it needs to perform an analysis under IFRS 15 to determine whether it is acting as a principal or an agent. IFRS 15 focuses on the transfer of control to determine how and when an entity is acting as a principal or an agent. In other words, does the entity control the specified good or service before that good or service is transferred to a customer?

IFRS 15 provides three indicators to inform the entity about its control assessment if that assessment is not determinative in itself. These three indicators are not weighted, and no single indicator alone is determinative of whether an entity is acting as a principal or agent. Instead, the Standard says that the indicators may be more or less relevant to the assessment of control, depending on the nature of the specified good or service and the terms and conditions of the contract. In addition, different indicators may provide more persuasive evidence in different contracts.

### Examples of the principal versus agent assessments

The following comprehensive example goes through a scenario where an entity concludes that it is acting as an agent. In its assessment, the entity identifies the specified good or service and then determines whether it controls the specified good or service before it is transferred to the customer. The entity considers the indicators to support the control assessment.

#### Example 3 - Arranging for the provision of goods or services (entity is an agent)

Entity A operates a website that connects customers to suppliers who sell and deliver goods directly to the customers. Entity A has contracts in place with the suppliers that entitle Entity A to a commission of 15% of the sales price when a good is purchased via the website. The suppliers set the prices and Entity A's website facilitates the customers' payments to the suppliers. Entity A requires payment upfront before orders are processed and does not allow for refunds. After arranging the transaction between the suppliers and customers and processing payments, Entity A has no further obligations.

#### Analysis

Entity A considers the following when assessing whether they are the principal or agent in sales transactions that take place on the platform:

Identification of the specified good or services to be provided to the customer:

- Entity A's website is a marketplace where suppliers offer their goods and customers purchase the goods offered by the suppliers
- The specified goods are the goods available for sale on the website

Control assessment:

- Entity A cannot direct the use of the goods at any point (eg Entity A is not able to direct the goods to another party)
- Entity A does not control the suppliers' inventory of goods used to fulfil the orders placed by customers

Entity A also considered the indicators of control laid out in IFRS 15:

- The supplier is primarily responsible for fulfilling the promise to provide the goods to the customer. Entity A is not required to fulfil the sale if the supplier fails to do so and is not responsible for customer satisfaction
- Entity A does not have inventory risk. It does not commit to obtain the goods from the supplier before the customer makes the purchase, and does not take responsibility for goods that are damaged or returned
- Entity A does not have the ability to set prices. Sales prices are set by the suppliers

Entity A therefore concludes that it does not control the specified goods before they are transferred to customers.

Based on these considerations Entity A concludes that it is an agent and its performance obligation is to arrange for the provision of goods by the supplier. When the entity satisfies its promise to arrange for the goods to be provided by the supplier to the customer (which, in this example, is when goods are purchased by the customer), the entity recognises revenue in the amount of the commission to which it is entitled.

As noted above, if a contract contains more than one specified good or service, an entity may be a principal for some goods or services and an agent for others. The following example illustrates where the entity concludes that it is acting as a principal and an agent in the same contract. In the assessment, the entity identifies the specified goods or services and then determines if it controls each specified good or service before they are transferred to the customer. The entity considers the indicators to support the control assessment.

#### **Example 4 – Entity is a principal and an agent in the same contract**

Entity B sells flights and hotel accommodation to its customers. Entity B books the flights directly with the respective airlines according to the customer's preferences. In return, Entity B receives a discount compared to the retail price at which the customers could book a flight directly with the airline. However, Entity B does not commit to purchase tickets from the airline before the customer books the holiday, and the airline sets the price that is charged to the end customer. The airline is responsible for fulfilling obligations to provide the flight and is responsible for resolving customer complaints.

In addition, Entity B has purchased room bookings at certain hotels, which it sells on to customers. These room bookings mean that the hotel cannot sell the specified rooms to other parties, and if Entity B is unable to sell the room booking to a customer the room cannot be returned to the hotel.

#### **Analysis**

Entity B sells flights and overnight hotel stays separately, ie the customer is free to choose the airline and combine it with a hotel of their choice from Entity B's inventory, or can book just a flight, or just a hotel.

In contracts where a customer purchases a flight and hotel booking, Entity B concludes that there are two specified goods in the contract – the flights and the hotel accommodation.

In this case, Entity B concludes that it acts as an agent with regard to the flights, as it does not have the power of control prior to the booking by the customer. Entity B is neither primarily responsible for providing the flight nor does it bear inventory risk, as a booking with the airline is only triggered by the customer's request. Although Entity B receives a reduced price for the booked flights, it has no pricing authority regarding the final price to the customer. Therefore, the price reduction has the character of a sales commission, and only this amount is shown as revenue.

Regarding the hotel overnight stays, on the other hand, Entity B controls the hotel accommodation prior to providing it to the customer, as they have previously purchased the room bookings from the hotels. Entity B bears inventory risk, as rooms not sold to customers can no longer be returned to the hotels. In return, Entity B has pricing power as it is free to set the resale price to its customers. In relation to the hotel service, Entity B therefore acts as a principal and recognises the room rate as revenue.

### Example 5 – Identifying the customer in a distributor relationship

Supplier A manufactures and sells equipment. Supplier A sells directly to end customers and also sells through a distributor.

In transactions with distributors, the distributor identifies the end customer, agrees to a price with the end customer for the equipment, sends notification of the agreed upon sales price back to the supplier, and the supplier has three days to accept or reject the price offered. If the supplier agrees to the end customer pricing, the supplier drop-ships the equipment to the end customer. When the equipment is drop-shipped, the distributor never takes control of the equipment (ie the distributor does not have legal title, physical possession or risks and rewards of ownership related to the equipment). Inventory returns by the end customer are made to Supplier A.

The invoice to the end customer is on Supplier A letterhead, but Supplier A is paid by the distributor upon shipment to the end customer and there is no further credit risk to Supplier A. The distributor takes on credit extension including, in some situations, working with the end customer to set up an instalment sale. Supplier A does not participate in any credit extension as it is paid by the distributor at shipment. The payment received by Supplier A from the distributor at the time of shipment is ‘net’ of distributor commissions (eg if the invoice to the customer is for CU10,000 and the distributor commission is 5%, upon shipment, the distributor remits CU9,500 (CU10,000 - CU10,000 × 5%) to Supplier A).

#### Analysis

Supplier A considers whether the distributor or the end customer is its customer and determines that the end customer, not the distributor, is its customer because it is primarily responsible for fulfilling the equipment ordered by the end customer. Supplier A also considers whether it is acting as a principal and therefore would record revenue of CU10,000, or if it is acting as an agent, in which case it would record revenue of CU9,500.

Supplier A determines that it controls the equipment and therefore is acting as a principal for the following reasons:

- Supplier A has the ability to reject the transaction if it does not accept the price negotiated by the distributor
- The end customer knows it is purchasing the equipment from Supplier A
- Supplier A has primary responsibility for fulfilling the contract and Supplier A accepts returns from the end customer, and
- The distributor never takes control of the equipment. Further, the distributor does not purchase the equipment until it has identified the end customer and, as a result, it has no inventory risk.

Supplier A records revenue at the gross amount of CU10,000. The fees retained by the distributor are akin to a finder’s fee or commission, and therefore the supplier should also consider whether the fees to the distributor are an incremental cost of obtaining the contract and whether the fee should be recorded as a deferred commission asset. In this particular example, because the contract is completed at the time the equipment is shipped, the commission is expensed.



### Reimbursement of out-of-pocket expenses

Another area where it is important to make an appropriate distinction between the role of the entity as a principal or agent is the reimbursement by a customer of out-of-pocket expenses incurred by an entity in connection with its performance under a contract with a customer. The entity will need to determine whether it is acting as a principal or an agent with respect to the related specified goods or services. In this determination, the entity should first identify the specified goods or services to be provided to the customer and then assess whether it controls the specified goods or services before they are transferred to the customer.

#### Example 6 – Reimbursable costs

Entity C is a law firm and is reimbursed by its client for out-of-pocket expenses including meals, transportation, and lodging incurred by the engagement team for travel required in the execution of the client’s legal services engagement.

Entity C identifies the specified goods and services as the meals, airfare, and lodging consumed by its staff in the performance of the legal services and concludes that it controls the specified goods or services as it is the entity that is primarily involved in selecting the nature of the specified goods and services and directly consumes the benefits from the meals, airfare, and lodging. The benefits of the specified services are not transferred to the customer; rather, Entity C controls the benefit of the meals, airfare, and lodging services, which it integrates into its performance of the legal services for which the client has contracted.

#### Analysis

Because Entity C concludes that it controls the specified goods or services, the customer’s reimbursement of these items is included in the contract price.

## IFRIC agenda decision on principal versus agent considerations

The IFRS Interpretations Committee (IFRIC) received an inquiry as to whether a reseller of software licences is a principal or an agent when applying IFRS 15. The inquiry related to very specific fact pattern with a particular contractual constellation between the software manufacturer, the end customer and the software reseller.

The IFRIC rejected the request in an agenda decision in May 2022, pointing to sufficient guidance in the IFRS 15 Application Guidance in IFRS 15. At the same time, however, the IFRIC took the opportunity to once again explain the two-step assessment process set out in IFRS 15 by identifying the specified goods or services to be provided to the customer and assessing whether it controls each specified good or service before that good or service is transferred to the customer.

In its agenda decision, the IFRIC made a detailed evaluation of the facts and circumstances in the specific case of the inquiry in order to show, by way of example, how an appropriate assessment can be made. Nevertheless, the IFRIC did not make a final judgement as to whether the entity in the fact pattern of the request should be classified as principal or agent. Instead, it pointed out that such a conclusive assessment could only be made by using management judgement considering all relevant facts and circumstances in the individual case.

### Practical insight – Individual assessment

The agenda decisions of the IFRIC always refer to the specific facts and circumstances of the requested item only. However, the agenda decision on the principal versus agent assessment at a software reseller clearly shows that such an assessment necessarily involves considerable management judgement. In each individual case, the reporting entity must carefully and comprehensibly weigh the arguments for and against a principal position against the background of all relevant facts and circumstances. The application guidance in IFRS 15 provides the appropriate criteria for such an assessment.

## 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](http://www.grantthornton.global/locations) to find your local member firm.