

STAFF PAPER

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Project	Revenue from Contracts with Customers		
Paper topic	Principal versus Agent Considerations (Redeliberations)		
CONTACT(S)	Mary Mazzella	msmazzella@fasb.org	+1 203 956 3434
	Scott A. Muir	samuir@fasb.org	+1 203 956 3478
	Raghava Tirumala	rtirumala@ifrs.org	+44 207 246 6953

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Purpose

1. The December 16, 2015 joint Board meeting of the FASB and the IASB is a decision-making meeting. The purpose of the Board meeting is to:
 - (a) Provide a summary of the feedback received on the proposed amendments to the application guidance and the illustrative examples on principal versus agent considerations in the FASB's proposed Accounting Standards Update, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)* and the IASB's Exposure Draft, *Clarifications to IFRS 15*.¹
 - (b) Provide alternatives for the Boards to consider in light of the feedback received and reach technical decisions with respect to those alternatives.
2. This memo should be read in conjunction with FASB Memo No. 8 and IASB Agenda Paper No. 7F, which include the FASB and the IASB comment letter

¹ For the convenience of the IASB and the FASB members, the proposed amendments to the Application Guidance on principal versus agent considerations have been set out in the Appendix of this paper.

feedback, respectively, on the proposed amendments to the principal versus agent guidance in the new revenue standard.

3. The FASB staff would intend for the FASB to complete redeliberations at the December 16, 2015 meeting and proceed to issuing an Accounting Standards Update for vote by written ballot.
4. The IASB staff would intend for the IASB to complete redeliberations of the proposed amendments to the principal versus agent guidance and make final decisions during this joint Board meeting.
5. This paper is structured as follows:
 - (a) Background
 - (b) Summary of the proposed amendments
 - (c) Staff Analysis of Feedback Received and Recommendations
 - (i) Specified Good or Service
 - (ii) Control Principle – Services
 - (iii) Control Principle and Indicators
 - (iv) Illustrative Examples
 - (d) Estimating Gross Revenue
 - (e) Staff Recommendation Summary
 - (f) Cost Benefit Analysis and Next Steps (FASB)

Background

6. When another party, in addition to the entity, is involved in providing goods or services to a customer, Topic 606/IFRS 15 requires the entity to determine whether it is:
 - (a) The principal in the transaction because it provides the good or service to the customer (recognizing as revenue the gross amount of consideration to

IASB Agenda ref	7G
FASB Agenda ref	9

which it expects to be entitled in exchange for those goods or services transferred); or

- (b) The agent because it arranges for the other party to provide the good or service (recognizing as revenue the fee or commission to which it expects to be entitled in exchange for arranging for the other party to provide its goods or services to the customer).

7. This determination is based on the notion of control. That is, an entity is a principal if it controls the good or service that is transferred to the customer. Paragraphs 606-10-55-37 through 55-40 [B35–B38] include guidance (including some indicators) to help an entity make that determination.

8. At its July 2014 meeting, the FASB-IASB Joint Transition Resource Group for Revenue Recognition (TRG) discussed issues relating to the guidance on principal versus agent considerations. Those issues were discussed jointly by the IASB and the FASB at the March 2015 joint Board meeting. At that meeting, the staff provided the Boards with an update about the ongoing research and outreach on principal versus agent considerations. The IASB met in May 2015 to discuss possible actions that it could take to resolve the issues. The FASB and the IASB met jointly in June 2015 and made the same tentative decisions on how to address the principal versus agent issues. Following the June 2015 joint Board meeting, both Boards issued Exposure Drafts of the proposed amendments. The FASB issued its proposed Update in August 2015 with comments due by 15 October 2015. The IASB issued its single Exposure Draft of all proposed clarifications to IFRS 15, including the proposed amendments to the guidance on principal versus agent considerations, in July 2015 with comments due on 28 October 2015. The proposed amendments to the guidance on principal versus agent considerations in the FASB proposed Update and the IASB Exposure Draft were converged. That is, both Boards proposed the same amendments to the guidance. Many comment letter respondents commended the Boards’ decision to maintain convergence on principal versus agent considerations and urged the Boards to issue final amendments to this guidance also on a converged basis.

Summary of the Proposed Amendments

9. The following is a summary of the proposed amendments that were included in the FASB's proposed Update and the IASB's Exposure Draft:
- (a) The Boards' proposed amendments to the guidance in paragraph 606-10-55-36 [B34] and to add paragraph 606-10-55-36A [B34A] to clarify that (i) the principal versus agent assessment is performed for each specified good or service (unit of account); and (ii) a specified good or service is a distinct good or service (or distinct bundle of goods or services).
 - (b) The Boards proposed the addition of the guidance in paragraph 606-10-55-37A [B35A] to help explain the application of the control principle in the context of services.
 - (c) The Boards proposed amendments to the guidance in paragraph 606-10-55-39 [B37] and the addition of paragraph 606-10-55-39A [B37A] to clarify the role of the indicators included to assist in the principal versus agent evaluation; to reframe the indicators so as to suggest when an entity is a principal because it controls a specified good or service before it is transferred to the customer, rather than to suggest when an entity is an agent; and to better demonstrate how each indicator relates to the control principle. Specifically, those proposed amendments would clarify:
 - (i) That the list of indicators provided is not an exhaustive (or all-inclusive) list and merely *support* the assessment of control. That is, the indicators assist in the evaluation of whether the entity controls the specified good or service before it is transferred to the customer, rather than override or replace the control evaluation.
 - (ii) How each indicator relates to the control principle by explaining how each indicator supports the assessment of control and removing the indicator about the entity's form of

IASB Agenda ref	7G
FASB Agenda ref	9

consideration being a commission, which the Board concluded has no relationship to the assessment of control.

(iii) That one or more indicators may be more or less relevant to the control evaluation in different contracts.

(d) The Boards proposed amendments to the principal versus agent examples in Topic 606 and IFRS 15, as well as to include some additional examples, to clarify the application of the principal versus agent guidance.

10. As was discussed in the June 2015 joint Board meeting, the proposed amendments are a *package* of amendments that were proposed *together* to resolve key issues identified with respect to the application of the principal versus agent guidance in Topic 606/IFRS 15. The effectiveness of the amendments proposed was dependent on the totality of the amendments. The amendments were developed with the intent to achieve the following objectives:

(a) Clarify the relationship between the control principle for the principal versus agent evaluation (that is, that an entity that is a principal controls the specified good or service before it is transferred to the customer) and the related indicators that are intended to support the control assessment.

(b) Clarify how control, in the context of the principal versus agent evaluation, applies to those types of transactions for which stakeholders are experiencing difficulties in applying the principal versus agent guidance (for example, service arrangements)

(c) Clarify the unit of account for the principal versus agent evaluation.

Staff Analysis of Feedback Received and Recommendations

11. The staff of each Board has prepared a separate memo summarizing the comment letter feedback from its respective respondents with respect to the proposed amendments to the principal versus agent guidance. Refer to Memo No. 8 for the FASB summary and Agenda Paper No. 7F for the IASB summary. Overall feedback to each Board's proposals was consistent between the two groups and

was generally favorable. For the most part, comments were of a more detailed nature, focusing on areas for which drafting might be improved, rather than comments expressing disagreement with the Boards' decisions. Therefore, the staff recommend that the Boards affirm their previous decisions. Because the proposed amendments were presented as a *package* to achieve the objectives described earlier in this memo, the staff recommend that the Boards affirm *all* of the proposed amendments.

12. In addition, the staff are recommending that the Boards make one additional amendment to the guidance. That amendment would eliminate the credit risk indicator from paragraph 606-10-55-39 [B37] based on the considerations discussed in more detail later in this memo.

Questions for the FASB and the IASB

1. Do the Boards affirm the proposed amendments to clarify that a specified good or service is the unit of account for which an entity would determine whether it is a principal or an agent?
2. Do the Boards affirm the clarifications that were proposed in paragraph 606-10-55-37A [B35A] to the application of the control principle in the context of services?
3. Do the Boards affirm the proposed amendments to the indicators that (a) reframe the indicators to indicate when an entity is a principal, (b) clarify how each indicator relates to the control principle for the evaluation, and (c) clarify that one or more indicators may be more or less relevant to the control evaluation in different contracts?
4. Do the Boards wish to eliminate credit risk as an explicit indicator as to whether an entity controls a specified good or service before it is transferred to the customer (that is, delete the indicator from paragraph 606-10-55-39 [B37])?

Questions for the FASB

5. Does the Board think that all relevant issues have been deliberated?
6. Have the Board members received sufficient information and analysis to make informed decisions on those issues? If not, what other information or analysis do they need?
7. Do the expected benefits of the changes justify the perceived costs of change?
8. Should the staff proceed to drafting an ASU for a vote by written ballot?

Specified Good or Service

13. Overall, most respondents to the Boards' proposals were supportive of the clarification that (a) the principal versus agent analysis is performed for each specified good or service; and (b) a specified good or service is a distinct good or service (or distinct bundle of goods or services) to be provided to a customer (refer to respective comment letter summaries for further details). Therefore, the staff recommend that the Board affirm its proposed amendments in this area.
14. A few respondents thought that it could be difficult in some cases to determine when the specified good or service is the "right" to a good or service or when it is the underlying good or service itself (for example, in the case of Example 47 whether the specified good or service is a right to the flight [the ticket] or the flight itself). Those respondents further suggest that application of the control principle may be significantly affected by that determination.
15. In considering the concerns expressed, the staff acknowledge there may be some judgment involved in identifying the specified good or service in some cases. However, the staff do not think there is a clear path to making that judgment simple in all cases. The staff, however, think the examples and the Basis for Conclusions provide some useful direction to stakeholders and could be, perhaps in final drafting, further improved in this regard. However, the staff continue to believe the concept of controlling a "right" is important to

applying a principal versus agent evaluation based on a concept of control, and therefore, do not think there is any technical decision to revisit as a result of these respondent comments. With respect to concepts that might further be exemplified or explained to *assist* in making judgments of this nature, consider the following:

- (a) In Example 47, the ticket broker does not itself have the productive resources to fulfill the service (for example, the entity in Example 47 is not an airline that has planes and/or pilots), and it cannot change or modify the service. The ticket broker does not obtain a customer and then obtain a flight service provider to fulfill its performance obligation to the customer to transport them from Point A to Point B. Rather, the ticket broker obtains tickets before a customer is identified for each of those tickets it obtains. The tickets represent specified rights to fly on specific flights. The ticket broker, therefore, has a right to fly, which is an asset:
 - (i) That the ticket broker can direct the use of—the ticket broker can use the ticket itself, sell the ticket to any customer it wishes, or allow the ticket to expire unused; and
 - (ii) From which the ticket broker can obtain substantially all the remaining benefits—the ticket broker can either consume the right or obtain all of the cash flows from sale of that right.

The ticket broker then transfers that right to the customer. Hence, the customer obtains from the ticket broker a specified asset (the ticket representing the right to fly on a specified flight) that the ticket broker previously controlled.

- (b) Based on this notion expressed above for Example 47, some have expressed that it is unclear why the specified good or service in Example 46A is the office maintenance services the customer receives rather than the “right” to those services. In the staff’s view, this is not necessarily a conceptual distinction, but rather, as will often be the case,

a determination reached based on the facts and circumstances of the contract. In Example 46A, the entity obtains the contract with the customer to provide the office maintenance services *before* it engages a maintenance services provider to fulfill its performance obligation to the customer, which is the opposite of the sequence of events in Example 47. Consequently, the entity has contracted with the customer to provide a specified service before it engages the third party. The fact that the entity subsequently engages a subcontractor (the third-party maintenance services provider) creates a right for the *entity* that it controls. The entity uses that right to direct the services provider to fulfill the entity’s performance obligation of maintenance services to the customer. However, the entity does not transfer *that* right to the customer. The customer has simply contracted for office maintenance services—it is indifferent to whether the third-party service provider, the entity, or any other subcontractor carries out the actual maintenance services. The entity retains control over its right to services from the third-party service provider (that is, the entity retains the right to utilize the services from the service provider as it sees fit—it can utilize the service provider to fulfill that customer contract, another customer contract, or to service its own facilities). In contrast, in Example 47, the customer is not indifferent to which ticket the ticket broker transfers to it; the customer wants the ticket broker to transfer a *specific* right that the customer then controls (that is, a ticket for a specific seat on a specific flight).

16. Although identifying the specified good or service may require judgment in some cases, the staff think that this is not a more difficult judgment than identifying an entity’s performance obligations outside the context of a principal versus agent evaluation. The staff note that the core “Step 2” guidance (paragraph 606-10-25-18 [26]) considers that the promised goods or services in a contract may include “rights” (for example, to goods or services purchased by an entity or to goods or services to be provided in the future).

17. Additionally, the staff note that the TRG has discussed numerous questions about the broader topic of identifying performance obligations which demonstrated the need for judgment (for example, Memo 12 - Identifying Promised Goods or Services, Memo 16 - Stand Ready Obligations, Memo 39 - Application of the Series Provision and Allocation of Variable Consideration, Memo 46 - Pre-Production Activities, and Memo 48 - Customer Options for Additional Goods or Services). Each of those discussions highlighted that identifying the promised goods or services (and the performance obligations) in a contract will require judgment in some cases (consistent with existing GAAP and IFRS). The determination of the specified good or service for purposes of applying the principal versus agent considerations guidance (for example, whether the specified good or service is a right to an underlying service or the underlying service itself) is no different in this regard.
18. A few respondents asked whether the proposed amendments affect the accounting for customer loyalty programmes in which another party is involved in providing the good or service to the customer. The staff think that the proposed amendments include sufficient guidance to assist entities in making judgements about whether an entity has granted loyalty points as a principal or as an agent. Whether the accounting for those arrangements would change, especially compared to previous IFRS, would depend upon the specific facts and circumstances.

Control Principle - Services

19. Many respondents commented that the addition of paragraph 606-10-55-37A [B35A] helped in clarifying how the control principle relates to services. In particular, clarifying that a principal can direct another party to perform a service for the customer on its behalf explains how an entity can control a service, even when another party actually performs the service (for example, in Example 46A regarding office maintenance services). It also links that explanation to the definition of control in paragraph 606-10-25-25 [33]. A principal directs the use of the other party's services to fulfill, or partially fulfill, its performance obligation

IASB Agenda ref	7G
FASB Agenda ref	9

to the customer. The staff recommends that the Board affirm its proposed amendments in this area.

20. A few respondents questioned whether the significant service of integration referred to in paragraph 606-10-55-37A(c) [B35A(c)] might be better described as an indicator of control, rather than as a scenario explaining when an entity is a principal. This was considered by the staff before the Boards' initial deliberations in June 2015. However, at that time the Boards decided that when the specified good or service is a combined item (for example, the specialized equipment in Example 46 or the hospital in Example 10 Case A) and the entity is providing a significant service of integrating all of the component goods and services necessary to deliver that combined item to the customer, then the entity is the principal for that specified, combined good or service. Fundamentally, paragraph 606-10-35-37A(c) [B35A(c)] is highlighting that when an entity is providing a significant integration service, it controls all of those component goods or services (that is, the entity directs the use of any such goods or services provided by another party to fulfill the combined performance obligation). It follows that if the entity controls all of the component goods or services, then it controls the combined good or service before it is transferred to the customer. This guidance was not framed as an indicator because the staff think that, in this scenario, there is no question that the entity controls the combined good or service before it is transferred to the customer. The staff think that any opportunity to provide more definitive guidance, rather than leaving it open to judgment, reduces cost and complexity and increases the operability and understandability of the guidance. As framed in the proposals, an entity in a situation, such as that in Example 46 or in Example 10 Case A, could reach a principal versus agent conclusion without having to further consider the remainder of the principal versus agent guidance provided. The staff continue to think the guidance proposed in paragraph 606-10-35-37A(c) [B35A(c)] makes the guidance more operable and understandable than the issued guidance (or any alternative presentation of this guidance, for example, as an indicator). Accordingly, we think the proposed guidance should be included in the final amendments in substantially the same form as it was proposed.

Control Principle and Indicators

21. Almost all of the respondents were supportive of clarifying that control is the single principle for the principal versus agent evaluation and better linking the indicators to that principle. Respondents almost universally agreed that reframing the indicators in the positive (that is, as indicators that support when the entity *controls* the specified good or service before it is transferred to the customer, rather than when the entity is an agent) is a substantive improvement to the guidance. Therefore, the staff recommend that the Boards affirm its proposed amendments in this regard.
22. In addition, subject to some drafting suggestions, respondents also generally agreed that the Boards' decision to provide additional guidance for each of the control indicators, which more clearly explains how those indicators relate to control of the specified good or service, is a substantive improvement to the guidance. Consequently, the staff also recommend that the Boards affirm their previous decisions to make those amendments.

Primarily responsible and inventory risk indicators

23. A few respondents suggested that the primarily responsible and inventory risk indicators should be identified as "stronger" or as more relevant than the other indicators. However, the staff do not think a specified weighting of the indicators would substantially reduce judgment in the analysis. The Boards have already proposed amendments in their respective proposals to delete the commission indicator and, below, the staff discuss the potential removal of the credit risk indicator. With those amendments, there would be fewer indicators to analyze and less of a need for specified weighting of the remaining indicators. Furthermore, the presence of a clear principle (based on control) for the principal versus agent evaluation in Topic 606/IFRS 15 reduces the need for any specific weighting of the indicators. Because there is a clearly articulated principle, the staff think it should be clear that the appropriate weighting (or relative importance to the evaluation) of the indicators (or any one of the indicators) in any given scenario

IASB Agenda ref	7G
FASB Agenda ref	9

should be based on their relevance in assessing whether the entity controls the specified good or service before it is transferred to the customer. Paragraph 606-10-55-39A [B37A] in the proposals stated that the relevance of the indicators may vary by scenario precisely for that reason. That is, in some scenarios, one or more of the indicators may provide more relevant information about whether the entity controls the specified good or service before it is transferred to the customer, while, in other scenarios, one or more different indicators (or none of the indicators) may provide information more relevant to making the control assessment. Because of this, the staff do not think it would improve the guidance to prescribe a stronger or a weaker weighting to one or more of the indicators that would apply in all scenarios.

Credit risk indicator

24. A number of respondents suggested that the Boards should eliminate the credit risk indicator from paragraph 606-10-55-39 [B37]. The standard, as issued, included the following indicator in paragraph 606-10-55-39(e) [B37(e)] that an entity may be an agent:

The entity is not exposed to credit risk for the amount receivable from a customer in exchange for the other party's goods or service.

25. The Exposure Drafts proposed to reframe the credit risk indicator as follows:

The entity is exposed to credit risk for the amount receivable from the customer in exchange for the specified good or service. For example, if the entity is required to pay the other party involved in providing the specified good or service regardless of whether it obtains payment from the customer, this may indicate that the entity is directing the other party to provide goods or service on the entity's behalf. However, in some cases, an agent may choose to accept credit risk as part of its overall service of arranging for the provision of the specified good or service.

26. Respondents that proposed removal of the credit risk indicator cited the following reasons:

- (a) An entity assesses whether it is principal or agent *after* it concludes that a contract exists and that collectibility of the amount to which it is entitled from its customer is probable. As a result, credit risk should be only a remote risk if the arrangement passes Step 1 of the revenue model.
- (b) Credit risk is factored into pricing between the parties and is not relevant to evaluating whether an entity controls a specified good or service.
- (c) The caveat included in the description of the indicator (“However, in some cases, an agent may choose to accept credit risk as part of its overall service of arranging for the provision of the specified good or service”) has led some respondents to conclude that the Boards view credit risk as a weaker indicator (that is, as compared to the other indicators). This suggests, in their view, that this indicator is not very useful to evaluating control.
- (d) This indicator is almost never persuasive in practice today (it was explicitly identified as a “weaker” indicator in previous U.S. GAAP) and does not appear to link to the control principle.

27. The credit risk indicator was carried forward into the new revenue standard from the risks and rewards model within existing U.S. GAAP and IFRS. Paragraph 605-45-10-13 includes the following indicator of gross reporting.

The entity has credit risk. If an entity assumes credit risk for the amount billed to the customer, that fact may provide **weaker evidence** that the entity has risks and rewards as a principal in the transaction and, therefore, that it should record revenue gross for that amount. Credit risk exists if

IASB Agenda ref	7G
FASB Agenda ref	9

an entity is responsible for collecting the sales price from a customer but must pay the amount owed to a supplier after the supplier performs, regardless of whether the sales price is fully collected. **[emphasis added]**

Similarly, paragraph 21 of the Illustrative Examples on IAS 18 *Revenue* states that:

... Features that indicate that an entity is acting as a principal include:

- (a) ...
- (d) the entity bears the customer's credit risk for the amount receivable from the customer.

28. As was explained to the Boards at the June joint Board meeting, some stakeholders had noted that the indicators in paragraph 606-10-55-39 [B37] are substantially the same as those used to apply the previous risks and rewards principle in Subtopic 605-45 and IAS 18. Therefore, some stakeholders asserted that it was unclear how the indicators correlate to the notion of control defined in paragraph 606-10-25-25 [33] (that is, how the indicators relate to determining whether an entity has the ability to direct the use of, and obtain substantially all the remaining benefits from, a specified good or service).

29. Those stakeholders think that retaining the credit risk indicator confuses the fact that the evaluation is based on control. To those stakeholders, the inclusion of the credit risk indicator in the guidance suggests that there may be either a different, or another, principle to consider (for example, an additional risk and rewards “overlay” to the evaluation). Stakeholders assert this despite the following discussion in the basis for conclusions on ASU 2014-09 / IFRS 15:

BC382. The nature of the entity's promise may not always be readily apparent. For that reason, the Boards included indicators in paragraph 606-10-55-39 [B37] 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 guidance in U.S. GAAP and IFRS. However, as noted in paragraph BC380, the indicators in Topic 606 [IFRS 15] have a different purpose than previous revenue recognition guidance in that they are based on the concepts of identifying performance obligations and the transfer of control of goods or services.

30. The staff and some stakeholders think that credit risk will almost always be a weaker indicator than the other indicators similar to how it was viewed under previous U.S. GAAP. The staff thinks that retaining the credit risk indicator may complicate the analysis, especially when the control evaluation may be less straightforward (for example, when other indicators relevant to the evaluation provide contradictory indications). The proposed amendments included the addition of guidance to explain how each indicator supports the assessment of control. The staff think that the indicators that would remain (after deletion of credit risk) better support the assessment of control. That is at least partially because the indicators that would remain are likely to be more relevant to the assessment of control and therefore more easily support the notion of control. Additionally, the remaining indicators are considered by most stakeholders to be stronger indicators of when an entity is a principal. Therefore, the staff think that the credit risk indicator should be removed from the guidance. Removal of the credit risk indicator should reduce some of the complexity in the principal versus agent analysis by eliminating an indicator that will typically be less (or not) relevant to the evaluation. More broadly, reducing the number of indicators, particularly eliminating an indicator that many view as weaker, will help to emphasize and focus entities on, not just the indicators, but the control principle itself (which the indicators are simply intended to support). Lastly, the staff understand that historically under U.S. GAAP, the credit risk indicator in Subtopic 605-45 has been problematic from the perspective of entities trying to use exposure to credit risk to override stronger evidence of agency. This might continue under Topic 606/IFRS 15 or be made worse because Topic 606/IFRS 15,

IASB Agenda ref	7G
FASB Agenda ref	9

unlike previous U.S. GAAP, will not specify credit risk as a “weaker” indicator. This, in the staff’s view, provides an additional reason to consider its elimination.

Illustrative Examples

31. At the June joint Board meeting, the Boards tentatively decided to amend Examples 45-48 and to include some additional examples. Respondents commented that the revisions and new examples were helpful and, improve the operability and understandability of the standard. The staff will continue to improve the drafting of those examples based on specific comments provided by respondents that may be helpful, but note that significant changes are not expected. Because any changes to the examples will likely be minor and would not be revisions that change the application of the guidance in any significant way, the staff are not asking for any technical decisions from the Boards on this topic. Rather, while subject to drafting improvements, the examples will continue to reflect the Boards’ technical decisions as discussed throughout this memo. The staff of each Board will work together during drafting to maintain convergence in the examples. Each Board will have an opportunity to review drafts of the language before signing a ballot.

Estimating Gross Revenue

32. During initial deliberations, the Boards were informed of existing diversity in practice in transactions in which an entity is a principal in a transaction but is (and expects to remain) unaware of the price charged to the customer for its goods or services by an intermediary. Each Board decided not to include the issue within the scope of their respective projects, in part, because stakeholders informed the Boards that the issue is not pervasive in practice. However, both Boards included some discussion in their respective Basis for Conclusions on this topic. The Basis for Conclusions discussion in each Board’s proposed Update/exposure draft on this topic is not converged. Each staff drafted their respective Board’s basis for deciding not to undertake standard setting on this issue.

33. Respondents provided a variety of comments related to the Basis for Conclusions discussion of this topic. The feedback provided was inconsistent. Some

respondents preferred that the Boards delete this discussion from the Basis for Conclusions. Other respondents requested that the Boards include the discussion in the authoritative guidance.

34. Both Boards describe in their respective Basis for Conclusions reasons for not undertaking standard setting on this issue. The staff has not received any new substantive information from stakeholders that would affect the Boards' previous decisions not to include the issue in the scope of this project. Including the issue in the scope of this project likely would require an amendment to the transaction price guidance. The staff do not think it is prudent to change the transaction price guidance at this point of the implementation phase for an issue that is narrow in practice. Rather, the staff think that it is important for the staff of each Board to work together when updating the Basis for Conclusions in the final Standard to ensure some measure of consistency in the discussion with the aim of ensuring that there is no conflicting information. In addition, in response to feedback from some stakeholders, the staff will ensure that the scope of the issue being described in the Basis for Conclusions is clear to stakeholders.

Staff Recommendation Summary

35. Almost all respondents commented favorably on the Boards issuing converged proposals and urged the Boards to enact final amendments that were similarly converged. Therefore, the staff recommend that the Boards move forward with finalizing the amendments on a converged basis.
36. In the Board memo from the June joint Board meeting, the staff of each Board commented on how their respective recommendations were influenced by the desire for convergence. That is, the FASB staff did not recommend some improvements that it might have proposed if the FASB was not considering this with the IASB. Similarly, the IASB staff did not think some of the amendments were essential to addressing stakeholder concerns about the guidance, but recommended proposing them to maintain convergence in this key area of the guidance. The staff continues to believe that it is important for the Boards to

IASB Agenda ref	7G
FASB Agenda ref	9

maintain convergence in issuing the final guidance on principal versus agent considerations.

37. Therefore, the staff of each Board recommend that the Boards reaffirm their previous proposals and *also* recommend that the Boards eliminate the credit risk indicator from paragraph 606-10-55-39 [B37] for the reasons outlined in the staff analysis.

FASB Only: Cost Benefit Analysis and Next Steps

38. The staff does not anticipate that entities will incur significant costs as a result of the amendments in the proposed Update and the additional amendment being recommended by the staff to remove the credit risk indicator because the amendments are to guidance that currently is not effective. Furthermore, comment letter feedback generally was positive and respondents thought the proposed amendments would represent an improvement to Topic 606. The objective of this project is to reduce the risk of diversity in practice before entities implement Topic 606, which should benefit financial statement users by providing more comparable information. Additionally, the amendments in this proposed Update should reduce the cost and complexity of applying Topic 606 both at transition and on an ongoing basis by improving the operability and understandability of the guidance.
39. After redeliberations have been completed, the staff will prepare Accounting Standards Update—Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net). A preballot draft will be distributed to Board members near the end of December. The staff plans to perform external review of the draft concurrently with the preballot review.

Appendix Proposed amendments to the Application Guidance

Principal versus agent considerations

606-10-55-36 [B34] When another party is involved in providing goods or services to a customer, the entity shall determine whether the nature of its promise is a performance obligation to provide the specified goods or services itself (ie the entity is a principal) or to arrange for those goods or services to be provided by the other party ~~to provide those goods or services~~ (ie the entity is an agent). 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 (see paragraphs 606-10-25-19 through 25-22 [27–30]). If a contract with a customer includes more than one specified good or service, an entity could be a principal for some specified goods or services and an agent for others.

606-10-55-36A [B34A] To determine the nature of its promise (as described in paragraph B34), the entity shall:

- (a) identify the specified goods or services to be provided to the customer (which, for example, could be a right to a good or service to be provided by another party (see paragraph 606-10-25-18 [26])).
- (b) assess whether it controls (as described in paragraph 606-10-25-18 [33]) each specified good or service before that good or service is transferred to the customer.

606-10-55-37 [B35] An entity is a principal if ~~the entity~~ it controls a promised the specified good or service before the entity transfers the that good or service is transferred to a customer. However, an entity is does not necessarily acting as a principal control a specified good if the entity obtains legal title of ~~a product that good~~ only momentarily before legal title is transferred to a customer. An entity that is a principal in a contract may satisfy a performance obligation by itself or it may engage another party (for example, a subcontractor) to satisfy some or all of a performance obligation on its behalf.

606-10-55-37A [B35A] When another party is involved in providing goods or services to a customer, an entity that is a principal obtains control of:

- (a) a good or another asset from the other party that it then transfers to the customer;
- (b) a right to a service to be performed by the other party, which gives the entity the ability to direct that party to provide the service to the customer on the entity's behalf; or
- (c) a good or service from the other party that it then combines with other goods or services in providing the specified good or service to the customer. If an entity provides a significant service of integrating goods or services provided by another party into the specified good or service for which the customer has contracted, it controls the specified good or service before that good or service is transferred to the customer. In that case, the entity first obtains control of the good or service from the other party and directs its use to create the combined output that is the specified good or service.

606-10-55-37A [B35B] When (or as) an entity that is a principal satisfies a performance obligation, the entity recognises revenue in the gross amount of consideration to which it expects to be entitled in exchange for ~~those~~ the specified goods or services transferred.

606-10-55-38 [B36] An entity is an agent if the entity's performance obligation is to arrange for the provision of the specified goods or services by another party. An entity that is an agent does not control the specified good or service provided by another party before that good or service is transferred to the customer. When (or as) an entity that is an agent satisfies a performance obligation, the entity recognises revenue in the amount of any fee or commission to which it expects to be entitled in exchange for arranging for ~~the other party to provide its~~ the specified goods or services to be provided by the other party. An entity's fee or commission might be the net amount of consideration that the entity retains after paying the other party the consideration received in exchange for the goods or services to be provided by that party.

606-10-55-38 [B37] Indicators that an entity ~~is an agent (and therefore does not control)~~ the specified good or service before it is provided transferred to a the customer include, but are not limited to, the following:

- (a) ~~another party~~ the entity is primarily responsible for fulfilling the ~~contract; promise to provide the specified good or service~~. This typically includes responsibility for the acceptability of the specified good or service. If the entity is primarily responsible for fulfilling the promise to provide the specified good or service, this may indicate that the other party involved in providing the specified good or service is acting on the entity's behalf.
- (b) ~~the entity does not have~~ has inventory risk before ~~or after the goods the specified good or service~~ have been ordered by transferred to a customer; during shipping or after that transfer (for example, on return); For example, if the entity obtains, or commits to obtain, the specified good or service before obtaining a contract with the customer, that may indicate that the entity has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the good or service before it is transferred to the customer.
- (c) ~~the entity does not have~~ has discretion in establishing prices for the ~~other party's goods or services and, therefore, the benefit that the entity can receive from those goods or services is limited;~~ specified good or service. Establishing the price that the customer pays for the specified good or service may indicate that the entity has the ability to direct the use of that good or service. However, an agent can have discretion in establishing prices in some cases. For example, an agent may have some flexibility in setting prices in order to generate additional revenue from its service of arranging for goods or services to be provided by other parties to customers.
- (d) ~~the entity's consideration is in the form of a commission; and~~
- ~~(e)~~(d) ~~the entity is not~~ the entity is exposed to credit risk for the amount receivable from a the customer in exchange for the other party's specified goods or services. For example, if the entity is required to pay the other party involved in providing the specified good or service regardless of whether it obtains payment from the customer, this may indicate that the entity is directing the other party to provide goods or services on the entity's behalf. However, in some cases, an agent may choose to accept credit risk as part of its overall service of arranging for the provision of the specified good or service.

606-10-55-39A [B37A] The indicators in paragraph 606-10-55-39 [B37] 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.

606-10-55-39 [B38] If another entity assumes the entity's performance obligations and contractual rights in the contract so that the entity is no longer obliged to satisfy the performance obligation to transfer the ~~promised~~ specified good or service to the customer (ie the entity is no longer acting as the principal), the entity shall not recognise revenue for that performance obligation. Instead, the entity shall evaluate whether to recognise revenue for satisfying a performance obligation to obtain a contract for the other party (ie whether the entity is acting as an agent).

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