



# Revenue: Agent or principal?

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It is at the core of accounting for any business activities to identify and report revenue from those activities correctly in the entity's financial statements. One of the questions that often arises in relation to revenue is whether amounts received should be accounted for as an entity's own revenue earned as a principal or rather as amounts received on behalf of another party who actually provided the goods or services to customers. The IFRS Interpretations Committee recently considered a question in this regard and published an agenda decision with its views.

It is at the core of accounting for any business activities to identify and report revenue from those activities correctly in the entity's financial statements. IFRS 15 *Revenue from Contracts with Customers* ('**IFRS 15**') establishes the principles to account for revenue. The accounting treatment of transactions depends on the terms of the contracts as well as relevant facts and circumstances. It involves many aspects that require judgement and the interpretation of the contract terms and circumstances by preparers.

#### **Principal vs agent question**

One area of IFRS 15 that is often the subject to judgement is whether an entity acts as a principal or agent in the transaction in terms of which it receives an amount. In simple terms, the question is really whether the entity should recognise and reflect the full amount received as its own revenue or whether it merely acts as an intermediary for another party who supplies the goods or services to the customer. In the latter case, the other party, the principal, reflects the amount as its revenue, while the intermediary, the agent, should only show its consideration from its principal as revenue.

IFRS 15 provides significantly more guidance on this question than its predecessor, IAS 18.

#### **Question to the IFRIC**

The IFRS Interpretations Committee ('**the IFRIC**') recently published an agenda decision on a question posed to it whether a reseller of software licenses was a principal or agent. The reseller in the fact pattern concluded a distribution agreement with a software manufacturer. This agreement gives the reseller the right to sell the standard software licenses to its customers. The reseller has discretion as to the pricing of the software sold to its customers. The reseller provides pre-sales advice to the customers to identify the software that meets their needs. If a customer decides to purchase the software, the reseller places an order with and pays the manufacturer, who then provides the reseller with the licenses in the name of

the customer. The manufacturer and customer enter into an agreement that governs the customer's right of use, warranty and term of the license. If the customer does not accept the software purchased by the reseller, the reseller may not return the unaccepted licenses to the software manufacturer.

#### **Analysis of the IFRIC response**

The IFRIC did not conclude whether the reseller in question acts as a principal or agent. The decision indicates that the conclusion depends on the specific facts and circumstances, including the terms and conditions of the relevant contracts. This requires judgement, which amongst others include an assessment of control of the software licenses by the reseller prior to transfer to the customer. Paragraphs B34 - B38 provide a framework to exercise this judgement. The entity's revenue disclosures should reflect the judgement applied. The IFRIC's approach arguably demonstrates the importance of performing a detailed and principle-based fact specific analysis whenever the question arises whether a person acts as agent or principal. There is no single factor that swings the assessment one way or another; the outcome always depends on the facts and circumstances of the specific case.

Although the IFRIC did not conclude on the outcome, its commentary on the overall approach should provide useful guidance that can be applied in other instances. The core principle in IFRS 15 is that an entity acts as a principal if it obtains control of the promised goods or services before transfer to the customer. If, after applying the principles and requirements of control, it remains unclear whether the entity acts as a principal or agent, one should resort to the factors in paragraph B37 of IFRS 15 to make the assessment. The decision again confirms that the relevance of these factors depend on the nature of the specified goods or services and the terms and conditions of the specific agreements. These factors were not intended as a checklist.

