

*Proposed Accounting Standards Update*

Issued: August 31, 2015  
Comments Due: October 15, 2015

Revenue from Contracts with Customers  
(Topic 606)

Principal versus Agent Considerations (Reporting Revenue  
Gross versus Net)

The Board issued this Exposure Draft to solicit public comment on proposed changes to Topic 606 of the *FASB Accounting Standards Codification*®. Individuals can submit comments in one of three ways: using the electronic feedback form on the FASB website, emailing written comments to [director@fasb.org](mailto:director@fasb.org), or sending a letter to “Technical Director, File Reference No. 2015-290, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116.”

The *FASB Accounting Standards Codification*<sup>®</sup> is the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. An Accounting Standards Update is not authoritative; rather, it is a document that communicates how the Accounting Standards Codification is being amended. It also provides other information to help a user of GAAP understand how and why GAAP is changing and when the changes will be effective.

### **Notice to Recipients of This Exposure Draft of a Proposed Accounting Standards Update**

The Board invites comments on all matters in this Exposure Draft and is requesting comments by October 15, 2015. Interested parties may submit comments in one of three ways:

- Using the electronic feedback form available on the FASB website at [Exposure Documents Open for Comment](#)
- Emailing a written letter to [director@fasb.org](mailto:director@fasb.org), File Reference No. 2015-290
- Sending written comments to “Technical Director, File Reference No. 2015-290, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116.”

Do not send responses by fax.

All comments received are part of the FASB’s public file. The FASB will make all comments publicly available by posting them to the online public reference room portion of its website.

An electronic copy of this Exposure Draft is available on the FASB’s website.

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# Proposed Accounting Standards Update

## Revenue from Contracts with Customers (Topic 606)

### Principal versus Agent Considerations (Reporting Revenue Gross versus Net)

August 31, 2015

Comment Deadline: October 15, 2015

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# Summary and Questions for Respondents

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## Why Is the FASB Issuing This Proposed Accounting Standards Update (Update)?

On May 28, 2014, the FASB and the International Accounting Standards Board (IASB) issued a converged standard on recognition of revenue from contracts with customers. In June 2014, the FASB and the IASB (collectively, the Boards) announced the formation of the FASB-IASB Joint Transition Resource Group for Revenue Recognition (TRG). One of the objectives of the TRG is to inform the Boards about potential implementation issues that could arise when organizations implement the new revenue standard. The TRG also helps stakeholders to better understand specific aspects of the new revenue standard. The TRG does not issue authoritative guidance. Instead, the Boards evaluate the feedback received from the TRG and other stakeholders to determine what action, if any, is necessary for each potential implementation issue.

One issue discussed by the TRG relates to when another party, along with the entity, is involved in providing a good or a service to a customer. In those circumstances, Topic 606 requires the entity to determine whether the nature of its promise is to provide that good or service to the customer (that is, the entity is a principal) or to arrange for the good or service to be provided to the customer by the other party (that is, the entity is an agent). The determination is based upon whether the entity controls the good or the service before it is transferred to the customer. Topic 606 includes indicators to assist in the principal versus agent evaluation.

Discussions at TRG meetings informed the Board about implementation issues related to the implementation guidance on principal versus agent guidance considerations, including:

1. Identifying the unit of account at which an entity should assess whether it is a principal or an agent
2. Identifying the nature of the good or the service provided to the customer (for example, whether it is a good, a service, or a right to a good or service)
3. Applying the control principle to certain types of transactions, such as service arrangements
4. Interaction of the control principle with the indicators provided to assist in the principal versus agent evaluation.

The Board decided to add a project to its technical agenda to improve Topic 606 to address those issues by reducing:

1. The risk of diversity in practice arising from inconsistent application of the principal versus agent guidance
2. The cost and complexity of applying Topic 606 both at transition and on an ongoing basis.

## Who Would Be Affected by the Amendments in This Proposed Update?

The amendments in this proposed Update would affect entities with transactions included within the scope of Topic 606. The scope of that Topic includes entities that enter into contracts with customers to transfer goods or services (that are an output of the entity's ordinary activities) in exchange for consideration.

## What Are the Main Provisions?

The core principle of the guidance in Topic 606 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps:

1. Identify the contract(s) with a customer.
2. Identify the performance obligations in the contract.
3. Determine the transaction price.
4. Allocate the transaction price to the performance obligations in the contract.
5. Recognize revenue when (or as) the entity satisfies a performance obligation.

The amendments in this proposed Update would not change the core principle of the guidance. The amendments in this proposed Update would clarify the implementation guidance on principal versus agent considerations.

When another party is involved in providing goods or services to a customer, an entity is required to determine whether the nature of its promise is to provide the specified good or service itself (that is, the entity is a principal) or to arrange for that good or service to be provided by the other party (that is, the entity is an agent). When (or as) an entity that is a principal satisfies a performance obligation, the entity recognizes revenue in the gross amount of consideration to which it expects to be entitled in exchange for the specified good or service transferred to the customer. When (or as) an entity that is an agent satisfies a performance obligation, the entity recognizes revenue in the amount of any fee or commission to which it expects to be entitled in exchange for arranging for the specified good or service to be provided by the other party.

An entity is a principal if it controls the specified good or service before that good or service is transferred to a customer. The guidance includes indicators to assist an entity in determining whether it controls a specified good or service before it is transferred to the customer. Considering one or more of the indicators often will be helpful in determining whether the entity controls the specified good or service before it is transferred to the customer. Depending on the facts and circumstances, the indicators may be more or less relevant to the assessment of control. Additionally, when the indicators are relevant to the assessment of control, one or more of the indicators may be more persuasive to the assessment than the other indicators.

The amendments in this proposed Update are intended to improve the operability and understandability of the implementation guidance on principal versus agent considerations by clarifying the following:

1. 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. 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.
2. An entity determines the nature of each specified good or service (for example, whether it is a good, a service, or a right to a good or service).
3. 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 that will be performed by another 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 combines with other goods or services to provide the specified good or service to the customer.
4. The purpose of the indicators in paragraph 606-10-55-39 is to support or assist in the assessment of control. The proposed amendments in paragraph 606-10-55-39A clarify that the indicators may be more or less relevant to the control assessment and that one or more indicators may be more or less persuasive to the control assessment, depending on the facts and circumstances.

Existing illustrative examples (Examples 45 and 46 in paragraphs 606-10-55-317 through 55-324 and Examples 47 and 48 in paragraphs 606-10-55-325 through 55-334) would be amended to clarify how to apply the implementation guidance on principal versus agent considerations. Additional illustrative examples (Example 46A in paragraphs 606-10-55-324A through 55-324G and Example 48A in paragraphs 606-10-55-334A through 55-334F) would be included to further assist stakeholders with applying the guidance.

## When Would the Amendments Be Effective?

The amendments in this proposed Update would affect the guidance in Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which is not yet effective. The effective date and transition requirements for the amendments in this proposed Update would be the same as the effective date and transition requirements in Topic 606.

## How Do the Proposed Provisions Compare with International Financial Reporting Standards (IFRS)?

Topic 606 and IFRS 15, *Revenue from Contract with Customers*, created common revenue recognition guidance for GAAP and IFRS. On July 30, 2015, the IASB issued an Exposure Draft, *Clarifications to IFRS 15*. The proposed amendments in that Exposure Draft to the application guidance on principal versus agent considerations are the same as the amendments in this proposed Update. Accordingly, the proposed amendments to the implementation guidance on principal versus agent considerations are converged.

## Questions for Respondents

The Board invites individuals and organizations to comment on all matters in this proposed Update, particularly on the issues and questions below. Comments are requested from those who agree with the proposed guidance as well as from those who do not agree. Comments are most helpful if they identify and clearly explain the issue or question to which they relate. Those who disagree with the proposed guidance are asked to describe their suggested alternatives, supported by specific reasoning.

**Question 1:** The proposed amendments to paragraph 606-10-55-36 clarify the unit of account (the “specified good or service”) at which an entity would determine whether it is a principal or an agent and clarify that an entity can be both a principal and an agent in a single contract. Would the proposed amendments improve the operability and understandability of the principal versus agent guidance in Topic 606? If not, please explain why and suggest alternatives.

**Question 2:** Paragraph 606-10-55-37A clarifies application of the control principle to certain types of arrangements by explaining what a principal controls before the specified good or service is transferred to the customer. Would the proposed amendments improve the operability and understandability of the principal versus agent guidance in Topic 606? If not, please explain why and suggest alternatives.

**Question 3:** The proposed amendments to paragraph 606-10-55-39 provide indicators of when an entity controls the specified good or service before it is transferred to the customer and, therefore, would be a principal. The amendments

also clarify the relationship of each indicator to the control principle in paragraph 606-10-55-37. Paragraph 606-10-55-39A was added to explain that the indicators may be more or less relevant to the principal versus agent assessment depending on the nature of the arrangement and that different indicators may provide more or less persuasive evidence about whether the entity controls the specified good or service before it is transferred to the customer in different contracts. Would the proposed amendments improve the operability and understandability of the principal versus agent guidance in Topic 606? If not, please explain why and suggest alternatives.

**Question 4:** Would the revisions to the principal versus agent illustrative examples (Examples 45 through 48) and the added illustrative examples (Examples 46A and 48A) improve the operability and understandability of the principal versus agent guidance in Topic 606? If not, please explain why and suggest alternatives.

# Amendments to the *FASB Accounting Standards Codification*<sup>®</sup>

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## Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–4. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is underlined, and deleted text is ~~struck out~~.

## Amendments to Section 606-10-55

2. Amend paragraphs 606-10-55-36 through 55-40 and add paragraphs 606-10-55-36A, 606-10-55-37A through 55-37B, 606-10-55-39A, with a link to transition paragraph 606-10-65-1, as follows:

### **Revenue from Contracts with Customers—Overall**

#### **Implementation Guidance and Illustrations**

##### **> > Principal versus Agent Considerations**

**606-10-55-36** When another party is involved in providing goods or services to a **customer**, the entity should determine whether the nature of its promise is a **performance obligation** to provide the specified goods or services itself (that is, 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~~ (that is, 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). 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** To determine the nature of its promise (as described in paragraph 606-10-55-36), the entity should:

- 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))
- b. Assess whether it controls (as described in paragraph 606-10-25-25) each specified good or service before that good or service is transferred to the customer.

**606-10-55-37** 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 ~~does is~~ 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. ~~When an entity that is a principal satisfies a performance obligation, the entity recognizes revenue in the gross amount of considerations to which it expects to be entitled in exchange for those goods or services transferred.~~ **[Content amended and moved to paragraph 606-10-55-37B]**

**606-10-55-37A** 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
- 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.

**606-10-55-37B** When (or as) an entity that is a principal satisfies a performance obligation, the entity recognizes revenue in the gross amount of consideration to which it expects to be entitled in exchange for the specified good or service these goods or services transferred. **[Content amended as shown and moved from paragraph 606-10-55-37]**

**606-10-55-38** An entity is an agent if the entity's performance obligation is to arrange for the provision of the specified good ~~goods~~ or service ~~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 recognizes 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.

**606-10-55-39** Indicators that an entity ~~is an agent (and therefore does not control~~ controls the specified good or service before it is provided transferred to the customer ~~a 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 has 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 a 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. Subparagraph superseded by Accounting Standards Update 2015-XX. The entity's consideration is in the form of a commission.
- e. The entity is ~~not~~ exposed to credit risk for the amount receivable from ~~a the customer in exchange for the other party's goods or services~~ 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 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** The indicators in paragraph 606-10-55-39 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.

**606-10-55-40** 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 (that is, the entity is no longer acting as the principal), the entity should not recognize revenue for that performance obligation. Instead, the entity should evaluate whether to recognize revenue for satisfying a performance obligation to obtain a contract for the other party (that is, whether the entity is acting as an agent).

3. Amend paragraph 606-10-55-93(p), with a link to transition paragraph 606-10-65-1, as follows:

**> Illustrations**

**606-10-55-93** The examples are organized as follows:

p. Principal versus Agent Considerations

Example 45—Arranging for the Provision of Goods or Services (Entity Is an Agent)

Example 46—Promise to Provide Goods or Services (Entity Is a Principal)

Example 46A—Promise to Provide Goods or Services (Entity Is a Principal)

Example 47—Promise to Provide Goods or Services (Entity Is a Principal)

Example 48—Arranging for the Provision of Goods or Services (Entity Is an Agent)

Example 48A—Entity is a Principal and an Agent in the Same Contract.

4. Amend paragraphs 606-10-55-316, 606-10-55-318, 606-10-55-323 through 55-324, 606-10-55-327 through 55-329, 606-10-55-333 through 55-334 and add paragraphs 606-10-55-318A through 55-318C, 606-10-55-323A through 55-323B, the heading preceding 606-10-55-324A, 606-10-55-324A through 55-324G and their related heading, 606-10-55-328A through 55-328C, 606-10-55-333A through 55-333B, and 606-10-55-334A through 55-334F and their related heading, with a link to transition paragraph 606-10-65-1, as follows:

**> > Principal versus Agent Considerations**

**606-10-55-316** Examples 45–~~48~~48A illustrate the guidance in paragraphs 606-10-55-36 through 55-40 on principal versus agent considerations.

**> > > Example 45—Arranging for the Provision of Goods or Services (Entity Is an Agent)**

**606-10-55-317** An entity operates a website that enables customers to purchase goods from a range of suppliers who deliver the goods directly to the customers. When a good is purchased via the website, the entity is entitled to a commission that is equal to 10 percent of the sales price. The entity's website facilitates

payment between the supplier and the customer at prices that are set by the supplier. The entity requires payment from customers before orders are processed, and all orders are nonrefundable. The entity has no further obligations to the customer after arranging for the products to be provided to the customer.

**606-10-55-318** To determine whether the entity's performance obligation is to provide the specified goods itself (that is, the entity is a principal) or to arrange for those goods to be provided by the supplier (that is, the entity is an agent), the entity ~~considers~~ identifies the nature of its promise specified good or service to be provided to the customer and assesses whether it controls that good or service before the good or service is transferred to the customer. Specifically, the entity observes that the supplier of the goods delivers its goods directly to the customer and, thus, the entity does not obtain control of the goods. Instead, the entity's promise is to arrange for the supplier to provide those goods to the customer. In reaching that conclusion the entity considers the following indicators from paragraph 606-10-39 as follows:

- a. ~~Subparagraph superseded by Accounting Standards Update 2015-XX. The supplier is primarily responsible for fulfilling the contract — that is, by shipping the goods to the customer.~~
- b. ~~Subparagraph superseded by Accounting Standards Update 2015-XX. The entity does not take inventory risk at any time during the transaction because the goods are shipped directly by the supplier to the customer.~~
- c. ~~Subparagraph superseded by Accounting Standards Update 2015-XX. The entity's consideration is in the form of a commission (10 percent of the sales price).~~
- d. ~~Subparagraph superseded by Accounting Standards Update 2015-XX. The entity does not have discretion in establishing prices for the supplier's goods and, therefore, the benefit the entity can receive from those goods is limited.~~
- e. ~~Subparagraph superseded by Accounting Standards Update 2015-XX. Neither the entity nor the supplier has credit risk because payments from customers are made in advance.~~

**[Content amended and moved to paragraph 606-10-55-318C]**

**606-10-55-318A** The website operated by the entity is a marketplace in which suppliers offer their goods and customers purchase the goods that are offered. Accordingly, the entity observes that the specified goods to be provided to customers that use the website are the goods provided by the suppliers, and no other promises are made to customers by the entity.

**606-10-55-318B** The entity concludes that it does not control the specified goods before they are transferred to customers that order goods using the website. The entity does not at any time have the ability to direct the use of the goods transferred to customers. For example, it cannot direct the goods to parties other than the customers or prevent the supplier from transferring those goods to the customers.

The entity does not control the suppliers' inventory of goods used to fulfill the orders placed by customers using the website.

**606-10-55-318C** ~~As part of~~ reaching that conclusion the entity considers the following indicators ~~from in~~ paragraph 606-10-55-39 ~~as follows~~. The entity concludes that these indicators provide further evidence that it does not control the specified goods before they are transferred to the customers:

- a. ~~The supplier is primarily responsible for fulfilling the contract—that is, by shipping the goods to the customer~~ promise to provide the goods to the customer. The entity is neither obliged to provide the goods if the supplier fails to transfer the goods to the customer nor responsible for the acceptability of the goods.
- b. ~~The entity does not take inventory risk at any time before or after the goods are transferred during the transaction because the goods are shipped directly by the supplier to the customer. The entity does not commit to obtain the goods from the supplier before the goods are purchased by the customer and does not accept responsibility for any damaged or returned goods.~~
- c. ~~The entity's consideration is in the form of a commission (10 percent of the sales price).~~
- c.d. ~~The entity does not have discretion in establishing prices for the supplier's goods and, therefore, the benefit the entity can receive from those goods is limited. The sales price is set by the supplier.~~
- e. ~~Neither the entity nor the supplier has credit risk because payments from customers are made in advance.~~

**[Content amended as shown and moved from paragraph 606-10-55-318]**

**606-10-55-319** Consequently, the entity 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 recognizes revenue in the amount of the commission to which it is entitled.

**> > > Example 46—Promise to Provide Goods or Services (Entity Is a Principal)**

**606-10-55-320** An entity enters into a contract with a customer for equipment with unique specifications. The entity and the customer develop the specifications for the equipment, which the entity communicates to a supplier that the entity contracts with to manufacture the equipment. The entity also arranges to have the supplier deliver the equipment directly to the customer. Upon delivery of the equipment to the customer, the terms of the contract require the entity to pay the supplier the price agreed to by the entity and the supplier for manufacturing the equipment.

**606-10-55-321** The entity and the customer negotiate the selling price, and the entity invoices the customer for the agreed-upon price with 30-day payment terms. The entity's profit is based on the difference between the sales price negotiated with the customer and the price charged by the supplier.

**606-10-55-322** The contract between the entity and the customer requires the customer to seek remedies for defects in the equipment from the supplier under the supplier's warranty. However, the entity is responsible for any corrections to the equipment required resulting from errors in specifications.

**606-10-55-323** To determine whether the entity's performance obligation is to provide the specified goods or services itself (that is, the entity is a principal) or to arrange for ~~another party to provide those goods or services to be provided by another party~~ (that is, the entity is an agent), the entity ~~considers the nature of its promise identifies the specified good or service to be provided to the customer and assesses whether it controls that good or service before the good or service is transferred to the customer.~~ The entity has promised to provide the customer with specialized equipment; however, the entity has subcontracted the manufacturing of the equipment to the supplier. In determining whether the entity obtains control of the equipment before control transfers to the customer and whether the entity is a principal, the entity considers the indicators in paragraph 606-10-55-39 as follows:

- a. ~~Subparagraph superseded by Accounting Standards Update No 2015-XX. The entity is primarily responsible for fulfilling the contract. Although the entity subcontracted the manufacturing, the entity is ultimately responsible for ensuring that the equipment meets the specifications for which the customer has contracted.~~
- b. ~~Subparagraph superseded by Accounting Standards Update No 2015-XX. The entity has inventory risk because of its responsibility for corrections to the equipment resulting from errors in specifications, even though the supplier has inventory risk during production and before shipment.~~
- c. ~~Subparagraph superseded by Accounting Standards Update No 2015-XX. The entity has discretion in establishing the selling price with the customer, and the profit earned by the entity is an amount that is equal to the difference between the selling price negotiated with the customer and the amount to be paid to the supplier.~~
- d. ~~Subparagraph superseded by Accounting Standards Update No 2015-XX. The entity's consideration is not in the form of a commission.~~
- e. ~~Subparagraph superseded by Accounting Standards Update No 2015-XX. The entity has credit risk for the amount receivable from the customer in exchange for the equipment.~~

**606-10-55-323A** The entity concludes that it has promised to provide the customer with specialized equipment. Although the entity has subcontracted the manufacturing of the equipment to the supplier, the entity concludes that the

development of the specifications and the manufacturing of the equipment are not distinct because they are not separately identifiable (that is, there is a single performance obligation). The entity is responsible for the overall management of the contract and, thus, provides a significant service of integrating those items into the combined output—the specialized equipment—for which the customer has contracted. In addition, these activities are highly interrelated; for example, if necessary modifications to the specifications are identified as the equipment is manufactured, the entity is responsible for communicating revisions to the supplier and for ensuring that any associated rework required conforms with the revised specifications. Accordingly, the entity identifies the specified good to be provided to the customer as the specialized equipment.

**606-10-55-323B** The entity concludes that it controls the specialized equipment before that equipment is transferred to the customer in accordance with paragraph 606-10-55-37A(c). The entity provides the significant integration service necessary to produce the specialized equipment and, therefore, controls the specialized equipment before it is transferred to the customer. The entity directs the use of the supplier’s manufacturing service in creating the combined output that is the specialized equipment. In reaching the conclusion that it controls the specialized equipment before it is transferred to the customer, the entity also observes that even though the supplier delivers the specialized equipment to the customer, the supplier has no ability to direct its use (that is, the supplier cannot decide to use the specialized equipment for another purpose or direct that equipment to another customer). The terms of the entity’s contract with the supplier prevent the supplier from directing the use of the specialized equipment by specifying that the equipment must be delivered to the customer. The entity also obtains the remaining benefits from the specialized equipment by being entitled to the consideration in the contract from the customer.

~~**606-10-55-324** The entity concludes that its promise is to provide the equipment to the customer. On the basis of the indicators in paragraph 606-10-55-39, the entity concludes that it controls the equipment before it is transferred to the customer. Thus, the entity concludes that it is a principal in the transaction. The entity does not consider the indicators in paragraph 606-10-55-39 because the evaluation above is conclusive without consideration of the indicators, and The entity recognizes revenue in the gross amount of consideration to which it is entitled from the customer in exchange for the specialized equipment.~~

**> > > Example 46A—Promise to Provide Goods or Services (Entity Is a Principal)**

**606-10-55-324A** An entity enters into a contract with a customer to provide office maintenance services. The entity and the customer define and agree on the scope of the services and negotiate the price. The entity is responsible for ensuring that the services are performed in accordance with the terms and conditions in the contract. The entity invoices the customer for the agreed-upon price on a monthly basis with 10-day payment terms.

**606-10-55-324B** The entity regularly engages third-party service providers to provide office maintenance services to its customers. When the entity obtains a contract from a customer, the entity in turn enters into a contract with one of those service providers directing the service provider to perform office maintenance services for the customer. The payment terms in the contracts with the service providers generally are aligned with the payment terms in the entity's contracts with customers. However, the entity is obliged to pay the service provider even if the customer fails to pay for any reason.

**606-10-55-324C** To determine whether the entity is a principal or an agent, the entity identifies the specified good or service to be provided to the customer and assesses whether it controls that good or service before the good or service is transferred to the customer.

**606-10-55-324D** The entity observes that the specified services to be provided to the customer are the office maintenance services and that no other promises are made to the customer.

**606-10-55-324E** The entity concludes that it obtains control of the right to those services (which will be performed by the service provider) 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. In addition, the entity concludes that the following indicators in paragraph 606-10-55-39 provide further evidence that the entity controls the office maintenance services before they are provided to the customer:

- a. The entity is primarily responsible for fulfilling the promise to provide office maintenance services. Although the entity has subcontracted the services to the service provider, the entity is responsible for the acceptability of the services (that is, the entity is responsible for fulfilment of the promise in the contract, regardless of whether the entity performs the services itself or engages a third-party service provider to perform the services).
- b. The entity has discretion in setting the price for the services to the customer.
- c. The entity has credit risk for the amount receivable from the customer in exchange for the office maintenance services. The entity is required to pay the service provider regardless of whether it obtains payment from the customer.

**606-10-55-324F** The entity observes that it does not commit to obtain the services from the service provider before obtaining the contract with the customer, nor does it maintain available resources to provide maintenance services (for example, staff, equipment, or supplies). Thus, the entity does not have inventory risk with respect to the office maintenance services. Nonetheless, the entity concludes that it controls the office maintenance services before they are provided to the customer on the basis of the evidence in paragraph 606-10-55-324E.

**606-10-55-324G** Thus, the entity is a principal in the transaction and recognizes revenue in the amount of consideration to which it is entitled from the customer in exchange for the office maintenance services.

**> > > Example 47—Promise to Provide Goods or Services (Entity Is a Principal)**

**606-10-55-325** An entity negotiates with major airlines to purchase tickets at reduced rates compared with the price of tickets sold directly by the airlines to the public. The entity agrees to buy a specific number of tickets and must pay for those tickets regardless of whether it is able to resell them. The reduced rate paid by the entity for each ticket purchased is negotiated and agreed in advance.

**606-10-55-326** The entity determines the prices at which the airline tickets will be sold to its customers. The entity sells the tickets and collects the consideration from customers when the tickets are purchased; therefore, there is no credit risk.

**606-10-55-327** The entity also assists the customers in resolving complaints with the service provided by the airlines. However, each airline is responsible for fulfilling obligations associated with the ticket, including remedies to a customer for dissatisfaction with the service.

**606-10-55-328** To determine whether the entity's performance obligation is to provide the specified goods or services itself (that is, the entity is a principal) or to arrange for another party to provide those goods or services to be provided by another party (that is, the entity is an agent), the entity considers the nature of its promise identifies the specified good or service to be provided to the customer and assesses whether it controls that good or service before the good or service is transferred to the customer. ~~The entity determines that its promise is to provide the customer with a ticket, which provides the right to fly on the specified flight or another flight if the specified flight is changed or cancelled. In determining whether the entity obtains control of the right to fly before control transfers to the customer and whether the entity is a principal, the entity considers the indicators in paragraph 606-10-55-30 as follows:~~

- a. Subparagraph superseded by Accounting Standards Update 2015-XX. ~~The entity is primarily responsible for fulfilling the contract, which is providing the right to fly. However, the entity is not responsible for providing the flight itself, which will be provided by the airline.~~
- b. Subparagraph superseded by Accounting Standards Update 2015-XX. ~~The entity has inventory risk for the tickets because they are purchased before they are sold to the entity's customers and the entity is exposed to any loss as a result of not being able to sell the tickets for more than the entity's cost.~~
- c. Subparagraph superseded by Accounting Standards Update 2015-XX. ~~The entity has discretion in setting the sales prices for tickets to its customers.~~

- d. Subparagraph superseded by Accounting Standards Update 2015-XX. As a result of the entity's ability to set the sales prices, the amount that the entity earns is not in the form of a commission but, instead, depends on the sales price it sets and the costs of the tickets that were negotiated with the airline.

**606-10-55-328A** The entity concludes that with each ticket that it commits to purchase from the airline, it obtains control of a right to fly on a specified flight (in the form of a ticket) that the entity then transfers to its customers. Consequently, the entity determines that the specified good or service to be provided to the customer is that right that the entity controls. The entity observes that no other promises are made to the customer.

**606-10-55-328B** The entity controls the right to each flight before it transfers that right to one of its customers because the entity has the ability to direct the use of those rights by deciding whether to use the tickets to fulfill contracts with customers and, if so, which contracts they will fulfill. The entity also has the ability to obtain the remaining benefits from those rights by either reselling the tickets and obtaining all of the proceeds from those sales or, alternatively, using the tickets itself.

**606-10-55-328C** The indicators in paragraph 606-10-55-39(b) through 55-39(c) also provide evidence that the entity controls the right to each flight before that right is transferred to the customer. The entity has inventory risk with respect to the tickets because the entity committed to obtain the tickets from the airlines before obtaining a contract with a customer to purchase the tickets. Accordingly, the entity is obliged to pay the airlines for those rights regardless of whether it is able to obtain customers to resell those tickets to or whether it can obtain a favorable price for those tickets. The entity also establishes the price that its customers will pay for the tickets.

**606-10-55-329** The entity concludes that its promise is to provide a ticket (that is, a right to fly) to the customer. On the basis of the indicators in paragraph 606-10-55-39, the entity concludes that it controls the ticket before it is transferred to the customer. Thus, the entity concludes that it is a principal in the transaction transactions with customers. The entity ~~and~~ recognizes revenue in the gross amount of consideration to which it is entitled in exchange for the tickets transferred to the customers.

**> > > Example 48—Arranging for the Provision of Goods or Services (Entity Is an Agent)**

**606-10-55-330** An entity sells vouchers that entitle customers to future meals at specified restaurants. These vouchers are sold by the entity, and the sales price of the voucher provides the customer with a significant discount when compared with the normal selling prices of the meals (for example, a customer pays \$100 for a voucher that entitles the customer to a meal at a restaurant that would otherwise cost \$200). The entity does not purchase vouchers in advance; instead, it

purchases vouchers only as they are requested by the customers. The entity sells the vouchers through its website, and the vouchers are nonrefundable.

**606-10-55-331** The entity and the restaurants jointly determine the prices at which the vouchers will be sold to customers. The entity is entitled to 30 percent of the voucher price when it sells the voucher. The entity has no credit risk because the customers pay for the vouchers when purchased.

**606-10-55-332** The entity also assists the customers in resolving complaints about the meals and has a buyer satisfaction program. However, the restaurant is responsible for fulfilling obligations associated with the voucher, including remedies to a customer for dissatisfaction with the service.

**606-10-55-333** To determine whether the entity is a principal or an agent, the entity ~~considers the nature of its promise and whether it takes control of the voucher (that is, a right) before control transfers to the customer~~ identifies the specified good or service to be provided to the customer and assesses whether it controls the specified good or service before that good or service is transferred to the customer. In making this determination, the entity ~~considers the indicators in paragraph 606-10-55-39 as follows:~~

- a. ~~Subparagraph superseded by Accounting Standards Update 2015-XX. The entity is not responsible for providing the meals itself, which will be provided by the restaurants.~~
- b. ~~Subparagraph superseded by Accounting Standards Update 2015-XX. The entity does not have inventory risk for the vouchers because they are not purchased before being sold to customers and the vouchers are nonrefundable.~~
- c. ~~Subparagraph superseded by Accounting Standards Update 2015-XX. The entity has some discretion in setting the sales prices for vouchers to customers, but the sales prices are jointly determined with the restaurants.~~
- d. ~~Subparagraph superseded by Accounting Standards Update 2015-XX. The entity's consideration is in the form of a commission, because it is entitled to a stipulated percentage (30 percent) of the voucher price.~~

**606-10-55-333A** The entity observes that the specified good or service to be provided to the customer is the right to a meal (in the form of a voucher) at a specified restaurant or restaurants, which the customer can use itself or transfer to another person. The entity also observes that no other promises are made to the customer.

**606-10-55-333B** The entity concludes that it does not control the right to the meal before that right is transferred to the customer. In reaching this conclusion, the entity principally considers the following:

- a. The vouchers are created only at the time that they are transferred to the customers and, thus, do not exist before that transfer. Therefore, the

entity does not at any time have the ability to direct the use of the vouchers or obtain substantially all of the remaining benefits from the vouchers before they are transferred to customers.

- b. The entity neither purchases nor commits to purchase vouchers before they are sold to customers. The entity also has no responsibility to accept any returned vouchers. Therefore, the entity does not have inventory risk with respect to the vouchers as described in paragraph 606-10-55-39(b).
- c. The entity does not provide a customer with the right to a meal and, then, contract with a restaurant to fulfill the entity's promise to provide that meal. Customers obtain vouchers for specific meals from restaurants that they select. In other words, the entity is not engaging the restaurants to provide a service of serving meals to customers on the entity's behalf as described in paragraph 606-10-55-39(a).

~~606-10-55-334 The entity concludes that its promise is to arrange for goods or services to be provided to customers (the purchasers of the vouchers) in exchange for a commission. On the basis of the indicators in paragraph 606-10-55-39, the entity concludes that it does not control the vouchers that provide a right to meals before they are transferred to the customers. Thus, the entity concludes that it is an agent in the arrangement. The entity and recognizes revenue in the net amount of consideration to which the entity will be entitled in exchange for the service arranging for the restaurants to provide vouchers to customers for the restaurants' meals, which is the 30 percent commission it is entitled to upon the sale of each voucher.~~

### **> > > Example 48A—Entity Is a Principal and an Agent in the Same Contract**

**606-10-55-334A** An entity sells services to assist its customers in more effectively targeting potential recruits for open job positions. As part of the contract with a customer, the customer agrees to obtain a license to access a third party's database of information on potential recruits. The entity arranges for this license with the third party, but the customer contracts directly with the database provider for the license. The entity collects payment on behalf of the third-party database provider as part of its overall invoicing to the customer. The database provider sets the price to the customer for the license and is responsible for providing technical support with the online application and providing credits to which the customer may be entitled for service down-time or other technical issues.

**606-10-55-334B** To determine whether the entity is a principal or an agent, the entity identifies the specified goods or services to be provided to the customer and assesses whether it controls those goods or services before they are transferred to the customer.

**606-10-55-334C** For the purpose of this Example, it is assumed that the entity concludes that its recruitment services and the database access are two distinct goods or services on the basis of its assessment of the guidance in paragraphs 606-10-25-19 through 25-22. Accordingly, the specified goods or services to be

provided to the customer are access to the third party's database and recruitment services.

**606-10-55-334D** The entity concludes that it does not control the access to the database before it is provided to the customer. The entity does not at any time have the ability to direct the use of the license because the customer contracts for the license directly with the database provider. The entity does not control access to the provider's database—it cannot, for example, grant access to the database to a party other than the customer or prevent the database provider from providing access to the customer.

**606-10-55-334E** As part of reaching that conclusion, the entity also considers the following indicators in paragraph 606-10-55-39. The entity concludes that these indicators provide further evidence that it does not control access to the database before that access is provided to the customer:

- a. The entity is not responsible for fulfilling the promise to provide the database access service. The customer contracts for the license directly with the third-party database provider, and the database provider is responsible for the acceptability of the database access (for example, by providing technical support or service credits).
- b. The entity does not have inventory risk because it does not purchase or commit to purchase, the database access before the customer contracts for database access directly with the database provider, and it does not maintain the resources necessary to provide the database access.
- c. The entity does not have discretion in setting the price for the database access with the customer because the database provider sets that price.

**606-10-55-334F** Thus, the entity concludes that it is an agent in relation to the third-party's database service. In contrast, the entity concludes that it is the principal in relation to the recruitment services because the entity performs those services itself and no other party is involved in providing them to the customer.

*The amendments in this proposed Update were approved for publication by the unanimous vote of the seven members of the Financial Accounting Standards Board.*

*Members of the Financial Accounting Standards Board:*

Russell G. Golden, *Chairman*  
James L. Kroeker, *Vice Chairman*  
Daryl E. Buck  
Thomas J. Linsmeier  
R. Harold Schroeder  
Marc A. Siegel  
Lawrence W. Smith

# Background Information and Basis for Conclusions

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## Introduction

BC1. The following summarizes the Board's considerations in reaching the conclusions in this proposed Update. It includes reasons for accepting certain approaches and rejecting others. Individual Board members gave greater weight to some factors than to others.

## Background Information

BC2. On May 28, 2014, the FASB issued Accounting Standards Update No. 2014-09, which introduced Topic 606, *Revenue from Contracts with Customers*, and the IASB issued IFRS 15, *Revenue from Contracts with Customers* (collectively, the new revenue standard). The new revenue standard is largely converged for GAAP and IFRS. In June 2014, the FASB and the IASB announced the formation of the FASB-IASB Joint Transition Resource Group for Revenue Recognition (TRG). One of the objectives of the TRG is to inform the Boards about potential implementation issues that could arise when organizations implement the new revenue standard. The TRG also helps some stakeholders to better understand specific aspects of the new revenue standard from others. The TRG does not issue guidance. Instead, the Boards evaluate the feedback received from the TRG and other stakeholders to determine what action, if any, is necessary for each potential implementation issue.

BC3. Reporting revenue gross versus net was discussed at the July 18, 2014 TRG meeting. The TRG discussed both the principal versus agent considerations guidance in the new revenue standard and the issue of determining the transaction price when an entity is a principal, but is unaware of the price charged to the customer for its goods or services by an intermediary (that is, whether an entity should estimate the price charged to the customer by the intermediary and recognize that amount as its gross revenue as a principal in the transaction). That discussion informed the Boards about potential challenges with consistent application of the new revenue standard. Following the TRG meetings, the FASB and the IASB directed their respective staffs to perform additional research and outreach on reporting revenue gross versus net. The focus of the additional research and outreach was to understand whether there were specific improvements each Board could make that would assist stakeholders with consistent application of the new revenue standard.

BC4. Both the FASB and the IASB agreed to make the amendments to the principal versus agent considerations guidance in this proposed Update. That is, both Boards agreed to clarify (a) the principle for determining whether an entity is a principal or an agent, (b) the relationship between control and the indicators in paragraph 606-10-55-39, (c) the application of control to intangible goods or services, and (d) the assessment of control of a service. Both Boards also agreed to amend existing examples and add new illustrative examples. As a result, the guidance to determine whether an entity is a principal or an agent will remain converged. The IASB proposed the amendments in its July 2015 Exposure Draft, *Clarifications to IFRS 15*. Both the FASB and IASB expect the proposed amendments will help reduce the cost and complexity of implementation by enhancing the operability and understandability of the guidance.

## Scope

BC5. The scope of the proposed guidance is the same as the scope of Topic 606 (see paragraphs 606-10-15-1 through 15-5).

## Principal versus Agent Considerations

BC6. When another party, in addition to the entity, is involved in providing goods or services to a customer, Topic 606 requires the entity to determine whether it is either:

- a. The principal in the transaction (recognizing as revenue the gross amount of consideration to which it expects to be entitled in exchange for providing the specified goods or services to the customer)
- b. The agent (recognizing as revenue the fee or commission for arranging for the specified goods or services to be provided by the other party to the customer).

Paragraphs 606-10-55-36 through 55-40 include guidance to help an entity make that determination.

BC7. The TRG discussed a number of issues regarding the guidance in paragraphs 606-10-55-36 through 55-40. Some stakeholders questioned whether control is always the basis for determining whether an entity is a principal or an agent and how the control principle and the indicators in paragraph 606-10-55-39 work together. Other stakeholders questioned how to apply the control principle to contracts involving intangible goods or services.

BC8. In the light of those discussions, the Boards discussed whether and how to clarify the principal versus agent guidance in paragraphs 606-10-55-36 through 55-40.

## Principle for Determining Whether an Entity Is a Principal or an Agent

BC9. Paragraph 606-10-55-36 requires an entity to determine whether it is a principal or an agent based on whether the nature of the entity's promise is a performance obligation to *provide* the specified goods or services itself (that is, the entity is a principal) or to *arrange* for those goods or services to be provided by another party (that is, the entity is an agent). Assessing whether the entity controls the specified good or service is the basis for determining the nature of the entity's promise.

BC10. The Boards observed that in order for an entity to conclude that it is providing the specified good or service to the customer, it must first control that good or service (as defined in paragraph 606-10-25-25). It would be difficult for an entity to provide the specified good or service to a customer if the entity does not first have (and control) that good or service to be provided. If an entity controls the specified good or service before that good or service is transferred to the customer, it is the principal in the transaction with the customer. If the entity does not control the specified good or service before it is transferred to a customer, it is not a principal in the transaction with the customer. The Boards noted that their considerations in this respect are explained in paragraph BC380 of Update 2014-09.

BC11. In addition, the Boards noted that an entity that itself manufactures a good or performs a service is always a principal if the entity transfers control of that good or service to another party. Such an entity does not evaluate whether it is a principal or an agent using the guidance in paragraphs 606-10-55-36 through 55-40 because the entity transfers the good or provides the service directly to its customer, without the involvement of another party. If the entity transfers a good or provides a service to an intermediary that is a principal in providing that good or service to an end customer (whether individually or as part of a distinct bundle of goods or services), the entity's customer is the intermediary.

BC12. Because of the concerns highlighted in the TRG discussions, the Boards decided to clarify the following aspects of the implementation guidance on principal versus agent considerations:

- a. The relationship between the control principle and the indicators in paragraph 606-10-55-39
- b. The application of the control principle to intangible goods or services.

BC13. Throughout the guidance on principal versus agent considerations, the Boards decided to refer to the *specified good or service* transferred to the customer (as in paragraph 606-10-55-36), rather than the *performance obligation*. This is because use of the term *performance obligation* would have been confusing if the entity is an agent. An agent's performance obligation is to arrange for goods or services to be provided by another party; it does not promise to provide the goods

or services itself to the end customer. Accordingly, the specified good or service to be provided to the end customer is not the performance obligation of the agent.

## The Relationship between Control and the Indicators in Paragraph 606-10-55-39

BC14. The Boards observed that the questions regarding the relationship between the assessment of control and the indicators of control in paragraph 606-10-55-39, at least in part, arise because the indicators in paragraph 606-10-55-39 are carried forward from Topic 605, Revenue Recognition, and IAS 18, *Revenue*. IAS 18 had a principle for this assessment (based on risks and rewards) that was different from the control principle in IFRS 15 and although Topic 605 did not explicitly include a principle, the indicators were understood to be indicators of risks and rewards. In addition, the structure of the analysis in Examples 45–48 in Topic 606 has added to the confusion.

BC15. The Boards' considerations (explained in paragraph BC382 of Update 2014-09) highlight that the indicators in paragraph 606-10-55-39 were included to support an entity's assessment of whether it controls a specified good or service before transfer in scenarios for which that assessment might be difficult. The indicators (a) do not override the assessment of control, (b) should not be viewed in isolation, (c) do not constitute a separate or additional evaluation, and (d) should not be considered a checklist of criteria to be met, or factors to be considered, in all scenarios. Considering one or more of the indicators often will be helpful, and, depending on the facts and circumstances, individual indicators will be more or less relevant or persuasive to the assessment of control.

BC16. The Boards acknowledged that the indicators are similar to those in Topic 605 and IAS 18 but also noted their considerations in this respect explained in paragraph BC382 of Update 2014-09. Paragraph BC382 explains that the Boards decided to carry over some of the indicators in previous revenue recognition standards even though those indicators have a different purpose in the new standard. In the new standard, the indicators support the concepts of identifying performance obligations and the transfer of control of goods or services. Accordingly, the Boards had expected that the conclusions about principal versus agent under Topic 606 could be different in some scenarios from those reached under the previous revenue recognition standards. Furthermore, the Boards observed that although exposure to risks and rewards alone does not give an entity control, exposure to risks and rewards can be a helpful factor to consider in determining whether an entity has obtained control.

BC17. The Boards considered whether the indicators in paragraph 606-10-55-39 should be amended to more clearly establish a link between the control principle and the indicators, ultimately deciding to propose the following:

- a. To reframe the indicators as indicators of when an entity controls a specified good or service before transfer, rather than as indicators that an entity does not control the specified good or service before transfer.
- b. To add guidance to explain how each indicator supports the assessment of control as defined in paragraph 606-10-55-39. This would help entities apply indicators that are similar to those in previous revenue recognition guidance but within the context of the control principle in Topic 606.
- c. To remove the indicator relating to the form of the consideration. Although that indicator might sometimes be helpful in assessing whether an entity is an agent, the Boards concluded that it would not be helpful in assessing whether an entity is a principal.
- d. To clarify that the indicators are not an exhaustive list and merely support the assessment of control—they do not replace or override that assessment. Different indicators might provide more persuasive evidence to support the assessment of control in different scenarios.

BC18. The FASB considered whether additional changes to the indicators, beyond those in BC17, might further clarify and make more operable the application of the control principle. For example, the FASB considered whether there were additional, or different, factors or criteria that might be determinative to the principal versus agent assessment that should be included in the guidance in addition to, or instead of, the indicators in paragraph 606-10-55-39. The FASB also considered whether, even if the indicators in paragraph 606-10-55-39 were mostly retained, additional changes differentiating them from the indicators in previous GAAP would help entities to understand and apply the different principle those indicators serve in Topic 606 (that is, different from the risks and rewards principle underlying previous GAAP).

BC19. Despite the FASB's view that some additional changes might further clarify the principal versus agent guidance in Topic 606, the FASB decided to propose more limited amendments that are converged with those that have been proposed by the IASB. The FASB concluded that there were significant benefits to all stakeholders in retaining converged principal versus agent guidance and that any benefits that might be obtained from the additional changes that were considered did not outweigh the significant benefits of retaining converged principal versus agent guidance. The FASB also observed that some of the benefits that might be obtained from those additional considered changes could also be obtained through stakeholder education.

## The Use of the Indicators in Paragraph 606-10-55-39 Rather Than the Indicators in Paragraph 606-10-25-30

BC20. Some stakeholders have questioned why the indicators in paragraph 606-10-55-39 are different from the indicators on the satisfaction of performance obligations (paragraph 606-10-25-30), noting that both sets of indicators relate to control.

BC21. The Boards observed that the indicators in paragraph 606-10-25-30 are indicators of the point in time at which the customer obtains control of the promised good or service. Accordingly, those indicators serve a different purpose than the indicators in paragraph 606-10-55-39. The indicators in paragraph 606-10-25-30 are not intended to indicate *whether* the customer obtains control of a promised asset—in the context of Topic 606 as a whole, it is assumed that the customer will obtain control of the promised asset at some point—instead, they are intended to indicate *when* the customer has obtained control. In contrast, the indicators in paragraph 606-10-55-39 are intended to indicate whether the entity controls a specified good or service at any point before that good or service is transferred to the customer.

## Applying Control to Intangible Goods or Services

BC22. The Boards observed that at least some of the difficulty that stakeholders have raised about the application of the control principle, in particular to intangible goods and services, is linked to challenges in identifying the specified good or service to be provided to the customer. The Boards observed that this also had frequently been a challenge for entities under previous revenue recognition guidance.

BC23. The principal versus agent considerations relate to the application of Step 2 of the revenue recognition model—*identify the performance obligations in the contract*. Appropriately identifying the good or service to be provided is a critical step in appropriately identifying whether the nature of an entity's promise is to act as a principal or an agent. When the appropriate specified good or service is identified, the assessment of control often is relatively straightforward, even in scenarios for which the specified good or service is an intangible good or a service. For example, the specified good or service to be provided to the customer could be:

- a. A right to goods or services (see paragraph 606-10-25-18). For example, the airline ticket (a right to fly) in Example 47 and the meal voucher (a right to a meal) in Example 48 in this proposed Update.
- b. A bundle of goods or services that are not distinct from each other (for example, the specialized equipment in Example 46 in this proposed Update).

BC24. The Boards observed that when the specified good or service to be provided to the customer is a right to goods or services to be provided in the future by another party, the entity would determine whether its performance obligation is a promise to provide a right to goods or services or whether it is arranging for the other party to provide that right. The fact that the entity will not provide the goods or services itself is not determinative. Instead, the entity evaluates whether it controls the right to goods or services before that right is transferred to the customer. In doing so, it is often relevant to assess whether the right is created

only when it is obtained by the customer, or whether the right to goods or services exists before the customer obtains the right. If the right does not exist before the customer obtains it, an entity (that is an intermediary) would be unable to control that right before it is transferred to the customer.

BC25. The Boards also observed that the specified good or service to which the control principle is applied should be a distinct good or service or a distinct bundle of goods or services. If individual goods or services are not distinct from each other, then they are merely inputs to a combined item and are each only part of a single promise to the customer. Accordingly, an entity should evaluate the nature of its promise in the contract (that is, to act as a principal or an agent) in the context of the promise to the customer, rather than for part of that promise. Consequently, in contracts in which goods or services provided by another party are inputs to a combined item (or items) for which the customer has contracted, the entity assesses whether it controls the combined item before that item is transferred to the customer.

BC26. When a specified good or service is a distinct bundle of goods or services, the principal versus agent analysis may, in some cases, be straightforward. The Boards concluded (in paragraph 606-10-55-37A(c)) that when an entity provides the significant service of integrating two or more goods or services into the combined output that is the specified good or service for which the customer contracted, it controls that specified good or service before it is transferred to the customer. The entity also controls the goods or services provided by the other party that are inputs to the specified good or service by directing their use to create the combined item. In that case, the inputs provided by the other party would be a fulfilment cost to the entity. In contrast, if a third party provides the significant integration service, then the entity's customer for its goods or services (which would be inputs to the specified good or service) is likely the other party.

BC27. Consequently, the Boards decided to clarify the thought process to be applied when assessing whether an entity is a principal or an agent by specifically requiring an entity to identify the specified good or service before applying the control principle to that specified good or service. The proposed additional paragraph (paragraph 606-10-55-36A) would achieve the following:

- a. It would provide a better framework (that is, clarify the thought process) to be applied when assessing whether an entity is a principal or an agent.
- b. It would emphasize the importance of appropriately identifying the specified good or service (which could be a right to a good or service to be provided by another party) that will be transferred to the customer.
- c. It would clarify that the specified good or service (that is, the unit of account for the principal versus agent evaluation) is each distinct good or service (or distinct bundle of goods or services). Accordingly, it also would clarify that because a contract with a customer could include more than one specified good or service, an entity could be a principal for one or more specified goods or services in a contract and an agent for others.

- d. It would emphasize that control (as defined in paragraph 606-10-25-25 is the determining factor when assessing whether an entity is a principal or an agent.

BC28. The FASB noted that, in many respects, the amendments to paragraphs 606-10-55-36 through 55-36A merely connect the principal versus agent guidance to other aspects of the revenue model in Topic 606. Therefore, including that guidance may not be essential to clarifying and improving the principal versus agent guidance, but would, nonetheless, be helpful. The FASB further observed that other areas of the implementation guidance in Topic 606, for example the guidance on licensing, include references to other aspects of the revenue model where the Boards concluded it was important to do so. In this case, the FASB concluded that the connections drawn between the principal versus agent guidance and those other aspects of the model are essential to applying the principal versus agent guidance appropriately, and therefore, including explicit guidance is important to ensure entities make those connections. The FASB also observed that, under previous GAAP (Topic 605, Revenue Recognition), entities frequently struggled to properly identify the deliverable when making principal versus agent evaluations, and therefore including clear guidance about identifying the specified good or service would represent an improvement to Topic 606 as compared with Topic 605.

## Assessment of Control of a Service

BC29. The TRG discussions highlighted concerns about the application of the control principle to services to be provided to a customer. Questions discussed included how an entity (other than the service provider) could control a service before that service is transferred to the customer because a service comes into existence only at the moment that it is delivered.

BC30. The Boards observed that an entity can control a service to be provided by another party when it controls the right to the specified services from the other party that will be provided to the customer. The entity then either transfers the right to the services to the customer or uses its right to direct the other party to provide the services to the customer on the entity's behalf (that is, to satisfy the entity's performance obligation in the contract with the customer). Determining whether the entity controls a right to a specified service requires consideration of the facts and circumstances. The Boards noted that contracts involving services provided by another party in which the entity is a principal can be broadly categorized as follows:

- a. Contracts in which an entity provides the customer with a right to a future service to be provided by another party, such as the right to a specified flight (in the form of a ticket) to be provided by an airline (as discussed in paragraph BC24).
- b. Contracts in which the service provided by the other party is not distinct from other goods or services promised to the customer, and the entity directs the use of that service to create the combined item that is the specified good or service for which the customer has contracted (as discussed in paragraphs BC25 through BC26). The proposed paragraph 606-10-55-37A(c) states that this scenario would exist whenever the entity provides a significant service of integrating the service provided by another party into the specified good or service for which the customer has contracted. Example 46 in this proposed Update illustrates this scenario.
- c. Contracts in which an entity engages (that is, directs) another party to provide the service to the customer on the entity's behalf in satisfying the entity's performance obligation. Example 46A in this proposed Update illustrates this scenario.

BC31. The Boards observed that determining whether an entity is a principal or an agent is more difficult in the third category of contracts. Having entered into a contract with a customer, the entity engages another party to satisfy a performance obligation within that contract on its behalf. In these contracts, the entity would assess whether it controls a right to the specified services. An entity could control the right to the specified services by entering into a contract with the service provider and defining the services to be performed by the service provider on the entity's behalf. In that scenario, the entity obtains the right to the services of the service provider and then directs the service provider to provide the services to the customer on the entity's behalf. This scenario is equivalent to the entity fulfilling the contract using its own resources rather than engaging a service provider to do so. The entity would remain responsible for the satisfactory provision of services in accordance with the contract with the customer. In other scenarios in which the specified services provided to the customer are provided by another party and the entity did not have the ability to direct those services, the entity would typically be an agent. In those scenarios, the entity is likely to be facilitating (and arranging for) the provision of services by the service provider rather than controlling the rights to the services that the entity then directs to the customer.

BC32. The Boards noted that paragraph 606-10-55-37 explains that an entity that is a principal in a contract may satisfy a performance obligation by itself or it may engage another party to satisfy some or all of a performance obligation on its behalf. The Boards decided to add further explanation to clarify the assessment of control of a service by explaining the scenarios in which a principal can control a service to be provided by another party. The Boards also decided to add Example 46A in this proposed Update to illustrate the application of control to services.

## Estimating Gross Revenue as a Principal

BC33. The Boards were informed of diversity in practice under previous GAAP (Topic 605) 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. The transactions in question do not include those for which the entity receives a fixed percentage (for example, 65 percent) of a contractually agreed “list price” from the intermediary, regardless of whether the intermediary increases or discounts that list price to the end customer. In those cases, the transaction price for the entity’s goods or services is known, and any incremental amount or discount is attributable to the intermediary.

BC34. With respect to those 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, the Boards were informed that some entities estimate the price charged to the customer by the intermediary and recognize that amount as their revenue, while other entities recognize the known amount to which they are entitled from the intermediary as their revenue. Some stakeholders asserted that the guidance in Topic 606 will not resolve that diversity in practice.

BC35. The FASB decided not to propose amendments to Topic 606 to address questions about those transactions. The Board’s rationale for this decision included:

- a. The narrow scope of the issue. Based on research and outreach, the issue is not pervasive and affects a limited number of entities and contracts.
- b. To maintain convergence with IFRS 15. The IASB chose not to make amendments to IFRS 15 for this issue. The reasons are described in paragraphs BC53 through BC56 in the IASB’s Exposure Draft, *Clarifications to IFRS 15*.
- c. The only practical solution to the issue identified to date would be through an amendment to the transaction price guidance in Section 606-10-32, Revenue from Contracts with Customer—Overall—Measurement. The Board is concerned there is a risk of unintended consequences of revising this core aspect of the guidance to address a narrow issue.
- d. The transaction price guidance in Section 606-10-32 addresses the accounting for this narrow set of transactions, as discussed in paragraphs BC36–BC38.

BC36. The Board’s view is that on the basis of the transaction price guidance in Section 606-10-32, the transaction price of a principal does not include the difference between the amount to which an entity is entitled from the intermediary and the amount charged by the intermediary to an end customer when the entity is (and expects to remain) unaware of the amount the intermediary charged to the end customer (for example, when the entity is entitled to \$1 per unit sold but is

unaware of whether the price charged to the customer is \$2 per unit, \$3 per unit, or something else). That is, the difference between the amount charged to the end customer and the amount to which the entity is entitled from the intermediary is not part of the negotiated exchange to which the entity is a party in those cases.

BC37. A key tenet of the concept of variable consideration in Topic 606 is that at some point the uncertainty in the transaction price ultimately will be resolved. For example, there eventually will be a payment or a royalty report that resolves the uncertainty. For the narrow set of transactions that gave rise to this issue, the uncertainty will never be resolved. Because the uncertainty is never expected to be resolved, the Board's view is that it is significant in concluding that the difference between the amount to which the entity is entitled from the intermediary and the amount charged by the intermediary to the end customer is not variable consideration. Accordingly, that amount is not part of the transaction price between the entity and the customer.

BC38. If the difference between the amount to which the entity is entitled from the intermediary and the amount charged by the intermediary to the end customer was part of the negotiated exchange to which the entity is party, the entity would be aware of that pricing. In considering this issue, the FASB observed that in some of the transactions that are the subject of this issue, the difference in pricing might be negative. That is, the customer pays the intermediary an amount that is less than what the intermediary is required to remit to the entity. Intermediaries sometimes price an entity's goods or services in this manner as a marketing incentive. When the difference is negative, it is typically for the benefit of the intermediary. This further supports the view that the difference is not part of the transaction price for the entity.

## Benefits and Costs

BC39. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC40. The Board does not anticipate that entities will incur significant costs as a result of the amendments in this proposed Update because it would amend guidance that currently is not effective. The objective of this proposed Update is to reduce the risk of diversity in practice before organizations 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.

## Amendments to the XBRL Taxonomy

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The provisions of this Exposure Draft, if finalized as proposed, would not require changes to the U.S. GAAP Financial Reporting Taxonomy (Taxonomy). Any stakeholders who believe that changes to the Taxonomy are required should provide their comments and suggested changes through [ASU Taxonomy Changes](#) provided at [www.fasb.org](http://www.fasb.org).