# The IFRS 15 Mole

***The IFRS 15 mole is back and has a new case! Katie Woods, PwC revenue specialist, is helping him get to the bottom of accounting for free gifts!***

FREE

### *Suspects*

Accounting for free gifts

### *Incident description*

Performance obligations (POs) are promises to a customer that arise every time they enter a contract to supply a good or service. Once the contract has been identified, the next step is to identify the POs. The 'incidents' start when not all of the POs are identified resulting in the incorrect measurement of revenue or recognition in the wrong period.

Not all POs need to be explicitly stated in the contract. Sometimes the buyer has a valid expectation of an 'extra' good or service being provided for example, a customary business practice or stated policy. This is an additional PO and needs to be considered in the application of IFRS 15.

The standard also helps by defining a PO as a good or service that is distinct. If a PO is distinct it is capable of being used on its own or together with resource available to the customer. So what have I found?

### *Facts*

Retailers transfer goods directly to their customers on or close to the date the goods are paid for, so many retailers believe that the implementation of IFRS 15 will be straightforward. This could be true.

Retailers, however, often offer incentives, like free goods, coupons or loyalty points to keep customers returning to their stores. They may need to take a closer look at the standard to consider the accounting consequences.

Many argue that the cost of the free goods is a marketing expenses. However, if a free good is promised to a customer, then it should be treated as a separate PO.

For example, if a customer buys a jumper and receives a voucher for a free scarf if they buy another jumper in the following month, part of the consideration for the initial jumper would need to be allocated to the scarf.

The future offer is referred to as a material right under IFRS 15. How much is allocated to each item (or PO), will depend on how the transaction price is allocated.

Loyalty points are in substance the same as a coupon or free good. Some of the consideration received in exchange for the goods sold at the time when the points are earned should be deferred until the points are exchanged for goods or services in the future.

The loyalty point is providing a right to a good or service to the customer, and therefore is a distinct PO. Again, the amount deferred will be a subject of one of my later investigations.

### *Recommendations*

The new revenue standard has a clear 5 step approach to determine when and how much revenue should be recognised. Management needs to think about all the promises being offered to the customer in step 2, identify POs, including those which are implicit. A promise deemed to be free or a marketing tool is probably a PO.

### *Further investigations*

Further investigation is required to identify all performance obligations in a transaction. A free good can be a performance obligation.