IFRS Accounting

Staff paper

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Project	**Transaction price (IFRS 9)**
Topic	**Potential annual improvement**
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Introduction

1. We have been informed about potential confusion arising from a reference in Appendix A of IFRS 9 *Financial Instruments* to the definition of 'transaction price' in IFRS 15 *Revenue from Contracts with Customers.* The potential for confusion arises because the term 'transaction price' is used in particular paragraphs of IFRS 9 with a meaning that is not necessarily consistent with the definition of that term in IFRS 15.

2. The IFRS Interpretations Committee (Committee) discussed this matter at its meeting in November 2022—see Agenda Paper 3C for that meeting.

3. The objective of this paper is:

   (a) to provide the International Accounting Standards Board (IASB) with background on the matter and staff analysis, including consideration of the Committee's discussion; and

   (b) to ask the IASB whether it agrees with our recommendation to include proposed amendments to IFRS 9 (see Appendix A) in its next *Annual Improvements to IFRS Accounting Standards Cycle* (annual improvements).

Structure of this paper

4. This paper includes:

   (a) Background information;

   (b) Staff analysis, including consideration of the Committee's discussion and transition requirements;

   (c) Staff recommendations and question for the IASB; and

   (d) Appendix A—recommended proposed amendments to IFRS 9.

Summary of staff recommendations

5. We recommend that the IASB:

   (a) propose amendments to IFRS 9, as set out in Appendix A to this agenda paper;

   (b) develop no specific transition requirements for these proposed amendments; and

   (c) include these proposed amendments in its next annual improvements cycle.

Background information

6. Paragraph 5.1.1 of IFRS 9 states [emphasis omitted]:

> Except for trade receivables within the scope of paragraph 5.1.3, at initial recognition, an entity shall measure a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

7. Several paragraphs in IFRS 9 use the term 'transaction price':

   (a) Paragraph 5.1.1A states:

> However, if the fair value of the financial asset or financial liability at initial recognition differs from the transaction price, an entity shall apply paragraph B5.1.2A.

(b) Paragraph 5.1.3 states:

> Despite the requirement in paragraph 5.1.1, at initial recognition, an entity shall measure trade receivables at their transaction price (as defined in IFRS 15) if the trade receivables do not contain a significant financing component in accordance with IFRS 15 (or when the entity applies the practical expedient in accordance with paragraph 63 of IFRS 15).

(c) Paragraph B5.1.1 states:

> The fair value of a financial instrument at initial recognition is normally the transaction price (ie the fair value of the consideration given or received, see also paragraph B5.1.2A and IFRS 13). […]

(d) Paragraph B5.1.2A states:

> The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price (ie the fair value of the consideration given or received, see also IFRS 13). If an entity determines that the fair value at initial recognition differs from the transaction price as mentioned in paragraph 5.1.1A, the entity shall account for that instrument at that date as follows:
>
> (a) at the measurement required by paragraph 5.1.1 if that fair value is evidenced by a quoted price in an active market for an identical asset or liability (ie a Level 1 input) or based on a valuation technique that uses only data from observable markets. An entity shall recognise the difference between the fair value at initial recognition and the transaction price as a gain or loss.

(b) in all other cases, at the measurement required by paragraph 5.1.1, adjusted to defer the difference between the fair value at initial recognition and the transaction price. After initial recognition, the entity shall recognise that deferred difference as a gain or loss only to the extent that it arises from a change in a factor (including time) that market participants would take into account when pricing the asset or liability.

8. Appendix A of IFRS 9 states (footnote omitted):

> The following terms are defined in paragraph 11 of IAS 32, Appendix A of IFRS 7, Appendix A of IFRS 13 or Appendix A of IFRS 15 and are used in this Standard with the meanings specified in IAS 32, IFRS 7, IFRS 13 or IFRS 15:
>
> (a) credit risk;
>
> (b) equity instrument;
>
> (c) fair value;
>
> (d) financial asset;
>
> (e) financial instrument;
>
> (f) financial liability;
>
> (g) transaction price.

9. Paragraphs 57–60 and B4 of IFRS 13 set out requirements for measuring fair value at initial recognition. Paragraph 57 of IFRS 13 states:

> When an asset is acquired or a liability is assumed in an exchange transaction for that asset or liability, the transaction price is the price paid to acquire the asset or received to assume the liability (an *entry price*). In contrast, the fair value of the asset or liability is the price that would be received to sell the asset or paid to transfer the liability (an exit price). Entities do not necessarily sell assets at the prices paid to acquire them. Similarly, entities do not

> necessarily transfer liabilities at the prices received to assume them.

10. Paragraph 58 of IFRS 13 states that 'in many cases the transaction price will equal the fair value'. Paragraph B4 of IFRS 13 describes situations in which the transaction price might not represent the fair value of an asset or a liability at initial recognition. Paragraph 60 of IFRS 13 states that 'if another IFRS [Accounting Standard] requires or permits an entity to measure an asset or liability initially at fair value and the transaction price differs from fair value, the entity shall recognise the resulting gain or loss in profit or loss unless that IFRS [Accounting Standard] specifies otherwise'.

11. Appendix A of IFRS 15 defines 'transaction price (for a contract with a customer)' as [emphasis omitted]:

> The amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties.

Question raised

12. The question raised is whether the reference to the definition of 'transaction price' in Appendix A of IFRS 9 should be removed to avoid potential confusion. Confusion may arise because the term 'transaction price' is used in particular paragraphs of IFRS 9 with a meaning that is not necessarily consistent with the definition of that term in IFRS 15.

Staff analysis

13. There are two ways in which IFRS 9 uses the term 'transaction price':

    (a) as defined in IFRS 15—in paragraph 5.1.3 of IFRS 9 in the context of trade receivables; and

(b) as the fair value of the consideration given or received—in paragraphs 5.1.1A, B5.1.1 and B5.1.2A of IFRS 9.

Transaction price as defined in IFRS 15

14. When IFRS 15 was issued in May 2014, it amended other IFRS Accounting Standards (Accounting Standards), including adding paragraph 5.1.3 of IFRS 9.

15. In July 2014 the IASB issued IFRS 9, which added to Appendix A of IFRS 9 a reference to the term 'transaction price', as defined in Appendix A of IFRS 15, and clarified that this term is used in IFRS 9 with the meaning specified in IFRS 15.

16. An entity applying paragraph 5.1.3 of IFRS 9 measures trade receivables at initial recognition at their 'transaction price (as defined in IFRS 15)' if the trade receivables do not contain a significant financing component in accordance with IFRS 15 (or when the entity applies a permitted practical expedient). The definition of transaction price in IFRS 15 is 'the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties'.

Transaction price as the fair value of the consideration given or received

17. Paragraph 5.1.1 of IFRS 9 states that an entity measures, at initial recognition, a financial asset or financial liability at its fair value plus or minus transaction costs (when applicable)—but makes an exception for trade receivables in the scope of paragraph 5.1.3 of IFRS 9. Paragraph B5.1.1 of IFRS 9 states that the fair value of a financial instrument at initial recognition is normally the transaction price (that is, the fair value of the consideration given or received) and includes references to paragraph B5.1.2A of IFRS 9 and IFRS 13. Paragraph B5.1.2A also references IFRS 13 and provides requirements for when an entity determines that the fair value at initial recognition differs from the transaction price.

Are the two uses of transaction price in IFRS 9 the same?

18. In determining the transaction price applying paragraph 47 of IFRS 15, an entity considers the terms of the contract and its customary business practices. The transaction price is the amount of consideration to which an entity *expects* to be entitled in exchange for transferring promised goods or services to a customer (excluding amounts collected on behalf of third parties). As set forth in paragraph 48 of IFRS 15, the nature, timing and amount of consideration promised by a customer affect the estimate of the transaction price and includes the effects of, for example, variable consideration, non-cash consideration and consideration payable to a customer. Therefore, transaction price as defined in IFRS 15 is an *entity-specific* measurement.

19. In contrast, as set forth in paragraph 2 of IFRS 13, the fair value (of the consideration received or paid) is a *market-based* measurement, not an entity-specific measurement. For some assets and liabilities, observable market transactions or market information might be available. For other assets and liabilities, observable market transactions and market information might not be available. However, the objective of a fair value measurement in both cases is the same—to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions (that is, the exit price at the measurement date from the perspective of a market participant that holds the asset or owes the liability).

20. In our view, therefore, it is evident based on the wording in each respective Accounting Standard that 'transaction price' as defined in IFRS 15 is not intended to be, and is not necessarily, the same as 'fair value of the consideration given or received'. We think it is also evident in the requirements of IFRS 9 when 'transaction price' refers to IFRS 15 and when it does not. In particular, paragraph 5.1.3 of IFRS 9 states that 'an entity shall measure trade receivables at their transaction price (as defined in IFRS 15)'; paragraph 5.1.1 of IFRS 9 states that paragraph 5.1.3 provides an exception from the requirement for an entity to measure, at initial recognition, a

financial asset or financial liability at its fair value plus or minus transaction costs (when applicable).

21. Therefore, it is unnecessary—and potentially confusing—to retain a reference to ‘transaction price’ (as defined in IFRS 15) in Appendix A of IFRS 9 and our preliminary view is to recommend deleting it (see Appendix A to this agenda paper).

22. We think that deleting ‘transaction price’ from Appendix A of IFRS 9 would be a minor correction. It would eliminate potential confusion and allow existing use of ‘transaction price’ terminology in IFRS 9 to stand on its own and reflect intended interactions between the requirements in IFRS 9, IFRS 13 and IFRS 15. It would also improve the understandability of Accounting Standards.

The Committee’s discussion

23. The Committee discussed this potential annual improvement at its November 2022 meeting. All Committee members agreed, or did not disagree, with our analysis and preliminary views.

24. A few Committee members suggested additional improvements. They said the IASB should consider amending paragraph 5.1.3 of IFRS 9, because this paragraph is not fully consistent with the requirements in IFRS 15 for the measurement, at initial recognition, of trade receivables that do not contain a significant financing component.

25. Paragraphs 105 and 108 of IFRS 15 state:

> 105 […] An entity shall present any unconditional rights to consideration separately as a receivable.
>
> 108 A receivable is an entity’s right to consideration that is unconditional. A right to consideration is unconditional if only the passage of time is required before payment of that consideration is due. […]

26. Paragraph 46 of IFRS 15 states:

> When (or as) a performance obligation is satisfied, an entity shall recognise as revenue the amount of the transaction price (which excludes estimates of variable consideration that are constrained in accordance with paragraphs 56–58) that is allocated to that performance obligation.

27. The right to consideration that is unconditional (a receivable) is not necessarily the same as the transaction price. Examples 39 and 40 that accompany IFRS 15 illustrate the relationship between the two amounts.

28. Example 40 states [emphasis added]:

> IE205 An entity enters into a contract with a customer on 1 January 20X9 to transfer products to the customer for CU150 per product. If the customer purchases more than 1 million products in a calendar year, the contract indicates that the price per unit is retrospectively reduced to CU125 per product.
>
> IE206 Consideration is due when control of the products transfer to the customer. Therefore, the entity has an *unconditional right to consideration (ie a receivable) for CU150 per product* until the retrospective price reduction applies (ie after 1 million products are shipped).
>
> IE207 In determining the transaction price, the entity concludes at contract inception that the customer will meet the 1 million products threshold and therefore estimates that the *transaction price is CU125 per product*. Consequently, upon the first shipment to the customer of 100 products the entity recognises the following:

Receivable	CU15,000[a]	
Revenue		CU12,500[b]
Refund liability (contract liability)		CU2,500

[a] CU150 per product × 100 products.

[b] CU125 transaction price per product × 100 products.

IE208 The refund liability (see paragraph 55 of IFRS 15) represents a refund of CU25 per product, which is expected to be provided to the customer for the volume-based rebate (ie the difference between the CU150 price stated in the contract that the entity has an unconditional right to receive and the CU125 estimated transaction price).

Staff analysis of the Committee input

29. We agree with the Committee members' views that paragraph 5.1.3 of IFRS 9 should be amended. IFRS 15 added paragraph 5.1.3 to IFRS 9 but did not use correct wording in doing so. In our view, the reference in paragraph 5.1.3 to the 'transaction price' as the basis for the initial measurement of trade receivables that do not contain a significant financing component was a minor oversight when IFRS 9 was amended by IFRS 15.

30. We therefore recommend replacing the words 'their transaction price (as defined in IFRS 15)' with 'the amount determined applying IFRS 15', which would remove the inconsistency between paragraph 5.1.3 of IFRS 9 and the requirements in IFRS 15. We think that it would be a minor correction to IFRS 9; it would help maintain consistent terminology between existing requirements and improve the understandability of Accounting Standards.

31. Based on the Committee's discussion, we do not think the amendments would change existing practice. Conversely, we think that the requirements in IFRS 15 for initial measurement of (trade) receivables that do not contain a significant financing

component are well understood, and entities recognise receivables at the amount that represents their unconditional right to consideration rather than at transaction price, which is determined to measure revenue.

Does this matter meet the annual improvements criteria?

32. Paragraphs 6.10–6.13 of the *Due Process Handbook* include the criteria for annual improvements. To meet these criteria, the proposed solution would need to be limited to:

    (a) clarifying the wording in an Accounting Standard, which involves either replacing unclear wording in existing Accounting Standards or providing requirements where an absence of requirements is causing concern; or

    (b) correcting relatively minor unintended consequences, oversights or conflicts between existing requirements.

33. We think that our proposed solution, as set out in Appendix A to this agenda paper, meets these criteria. As we explained earlier, we think that amending paragraph 5.1.3 of IFRS 9 would correct a relatively minor oversight between existing requirements and deleting the reference to 'transaction price' (as defined in IFRS 15) from Appendix A to IFRS 9 would improve the understandability of the Accounting Standard. These amendments would maintain consistency with the principles and requirements in IFRS 15 and would not propose a new (or change an existing) principle or requirement.

Transition requirements

34. Our proposed amendments to paragraph 5.1.3 of (and Appendix A to) IFRS 9 do not change or add requirements but help maintain consistency between existing requirements. We do not expect any change in practice arising from these proposed amendments or a material effect on entities' financial statements.

35. In the absence of any specific transition requirements, an entity would apply the proposed amendment retrospectively in accordance with paragraph 19(b) of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

Staff recommendations and question for the IASB

36. Based on our analysis in paragraphs 6–33 of this agenda paper, we recommend the IASB, as part of its next annual improvements cycle, amend paragraph 5.1.3 of (and Appendix A to) IFRS 9, as set out in Appendix A to this agenda paper.

37. Based on our analysis in paragraphs 34–35, we recommend the IASB develop no specific transition requirements.

Question for the IASB
Does the IASB agree with our recommendations: a. to propose amendments to IFRS 9 as set out in Appendix A to this agenda paper; b. to develop no specific transition requirements for these proposed amendments; and c. to include these proposed amendments in its next annual improvements cycle?

Appendix A—recommended proposed amendments to IFRS 9

A1. Our proposed amendments would revise wording in paragraph 5.1.3 of IFRS 9 and delete the reference to 'transaction price'—and the associated references to IFRS 15—from Appendix A of IFRS 9. New text is underlined and deleted text is struck through.

> 5.1.3 Despite the requirement in paragraph 5.1.1, at initial recognition, an entity shall measure trade receivables at ~~their transaction price (as defined in~~ the amount determined applying IFRS 15~~)~~ if the trade receivables do not contain a significant financing component in accordance with IFRS 15 (or when the entity applies the practical expedient in accordance with paragraph 63 of IFRS 15).
>
> …
>
> **Appendix A**
>
> **Defined terms**
>
> …
>
> The following terms are defined in paragraph 11 of IAS 32, Appendix A of IFRS 7~~,~~ or Appendix A of IFRS 13 ~~or Appendix A of IFRS 15~~ and are used in this Standard with the meanings specified in IAS 32, IFRS 7~~,~~ or IFRS 13 ~~or IFRS 15~~:
>
> (a) credit risk;[3]
>
> (b) equity instrument;
>
> (c) fair value;
>
> (d) financial asset;
>
> (e) financial instrument;
>
> (f) financial liability~~;~~.
>
> ~~(g) transaction price.~~
>
> [3] This term (as defined in IFRS 7) is used in the requirements for presenting the effects of changes in credit risk on liabilities designated as at fair value through profit or loss (see paragraph 5.7.7).