

**БУХГАЛТЕРСЬКИЙ ОБЛІК, АНАЛІЗ ТА АУДИТ**

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**CUSTOMER LOYALTY PROGRAMMES ACCOUNTING ISSUES  
(SELLER'S SIDE)****ПРОБЛЕМИ ОБЛІКУ ОПЕРАЦІЙ  
В РАМКАХ ПРОГРАМ ЛОЯЛЬНОСТІ КЛІЄНТІВ (З БОКУ ПРОДАВЦЯ)**

The article provides a brief overview of national and international standards for accounting discounts compared with bonuses accounting. While domestic bookkeepers still treat the costs of redeeming bonuses as selling/marketing expenses, IFRIC 13 'Customer Loyalty Programmes' since 2007 has constituted the procedure of reporting information about the nature, amount and timing of revenue and cash flows under such program. In subsequent years in accordance with IFRS 15 'Revenue from contracts with customers', the procedure of bonuses accounting was supplemented by the introduction of additional variables that must be taken into consideration – uncertainty and material right. The new standard introduces a five-step approach to bonus accounting, the last two of which regulate the allocation of the contract price to individual performance obligations and the recognition of income upon performance of obligations. All steps related to bonus accounting are illustrated with examples.

**Key words:** Customer loyalty program, accounting, discount, bonus, allocated price, IFRS 15 'Revenue from contracts with customers'.

Стаття присвячена аналізу різних підходів до вирішення проблем бухгалтерського обліку в рамках Програм лояльності клієнтів (бонусних програм). У роботі представлено короткий огляд національних та міжнародних стандартів обліку знижок у порівнянні з обліком бонусів, які називаються в IFRIC 13 «Программи лояльности клиентов» «нарахуваннями за лояльність», а в МСФЗ 15 «Дохід від контрактів з клієнтами» – як «бали». У той час як вітчизняні бухгалтери все ще розглядають витрати на погашення бонусів як маркетингові витрати без створення будь-яких резервів для майбутніх продажів із знижками, Комітет з тлумачень міжнародної фінансової звітності ще з 2007 року запровадив спеціальну процедуру подання інформації про характер, суму та терміни визнання доходу продавця, а також регламентував облік грошових потоків у процесах реалізації програм лояльності клієнтів. У наступні роки Рада з міжнародних стандартів бухгалтерського обліку, підтверджуючи раніше узгоджені принципи обліку бонусів, поповнила формулу розрахунків додатковими змінними, які необхідно брати до уваги, а саме: термінами «невизначеність» та «матеріальне право»; останнє було визначене як право, що дає клієнту можливість придбати додатковий товар або послугу за ціною, нижчою, ніж її окрема продажна ціна, за умови, що клієнт не отримає це право без укладання первинного договору купівлі-продажу в рамках програм лояльності клієнтів. Новим стандартом передбачений п'яти кроковий підхід до обліку операцій, пов'язаних з наданням бонусів: ідентифікація контракту, визначення окремих зобов'язань щодо виконання, визначення ціни контракту, розподіл ціни контракту на різні зобов'язання щодо виконання, визнання доходу при виконанні зобов'язань. Застосовуючи МСФЗ 15, суб'єкт господарювання має обліковувати одну частину, що відноситься до продажу основного продукту, як дохід на момент продажу, тоді як друга частина, що відноситься до бонусів, має бути облікована як зобов'язання за контрактом (своєї роду авансовий платіж). Усі кроки, пов'язані з обліком бонусів відповідно до МСФЗ 15, проілюстровані на конкретних прикладах.

**Ключові слова:** програма лояльності клієнтів, МСФЗ 15 «Дохід від договорів з клієнтами», облік, знижка, бонус, розподілена ціна.

В статье представлен краткий обзор национальных и международных стандартов учета скидок по сравнению с учетом бонусов. В то время как отечественные бухгалтеры все еще рассматривают расходы при предоставлении бонусов как расходы на продажу/маркетинг, положениями КТМФЗ 13 «Программы лояльности клиента» была введена новая процедура представления информации о характере, сумме и сроках признания дохода и денежных потоков в рамках таких программ. В последующие годы в соответствии с МСФО 15 'Доход от договоров с клиентами' процедура учета бонусов была дополнена введением дополнительных переменных, которые необходимо учитывать – неопределенность и материальное право. Новый стандарт вводит пятишаговый подход к операциям с предоставлением бонусов, два последних из которых регулируют распределение цены контракта на отдельные обязательства по выполнению и признание дохода при выполнении обязательств. Все шаги, связанные с учетом бонусов, проиллюстрированы примерами.

**Ключевые слова:** программа лояльности клиентов, МСФО 15 «Доход от договоров с клиентами», учет, скидка, бонус, распределенная цена.

**Problem statement.** Conventional Customer Loyalty Programmes definition is 'a marketing strategy designed to encourage customers to continue to shop at or use the services of a business associated with the program' [1].

In accounting we can interpret these programs in the function of their economic essence, either as a price decrease at the moment of sale or as two interrelated pledges of the seller: to provide a good/service on the spot and a discount for future purchase. The issue with accounting in the framework of second option is complicated by the uncertainty of the second event taking place and timeframe of it (if any). Different approaches to tackling this problem on the international level have been already attempted several times: in 2007 was issued IFRIC 13 'Customer Loyalty Programmes', in 2011 – IFRS 13 'Fair Value Measurement' and in 2018 IFRS 15 'Revenue from contracts with customers' became valid. But in Ukraine the problems of bonus accounting are still considered to be nonsignificant.

**Analysis of recent research and publications.** In academic literature there is not a huge number of papers, addressing Customer Loyalty Programmes. Those being published in most instances are focused either on the discussion of an economic essence of the program (it being titled as a bribe/kickback to the customer or a subsidy for customer [2]) or on the possible customers' violation of privacy (abuse of customers' personal data [3]) or on the comparative advantages/disadvantages of different types of programs. One more object of interest – efficiency of such programs: some experts complain that such programs discount goods to those who are buying them anyway [4].

Typical problems of accounting usually are outlined in international guidelines, including IAS 19 'Revenue', IFRIC 13 'Customer Loyalty Programmes', IFRS 13 'Fair Value Measurement' and IFRS 15 'Revenue from contracts with customers'.

**The purpose of this paper** is to disclose problems of transactions accounting (seller's

side) in different types of Customer Loyalty Programmes (CLP). As an illustrative example of these problems and different approaches to their solution, a case study of sales operation accounting of an item with the price of \$100 with discount or bonus is under examination.

**Research results.** Customer loyalty programmes is not a new phenomenon – they have been in use since 1896, when Sperry and Hutchinson Company started to sell their S&H Green Stamp. As from then they became the most popular tool of marketing: in order to attract new and retain today's customers sellers are proposing their customers variety of loyalty points, coupons, vouchers, discounts, bonuses, freebies, miles etc. For now, we can see dozens of different CLP, varying by the type of discounting, forms of bonuses, terms of validity, availability of tiers and number of businesses operating within it (in other words – participation of third parties). To analyze the problems of accounting of such generosity it is necessary to start with the dissection of the wide variety of CLP into generic types.

In this paper classification of CLP is presented from the accounting point of view.

The main criterion of CLP classification from the standpoint of a bookkeeper is availability of third parties. This paper limits itself with the most streamlined form, when CLP is carried out by one business entity – whether it is one shop or the whole sales network.

The simplest form of CLP from the accounting stand is *discounting program*: the customer is presented with a discount card, which provides him/her the right to buy some goods (receive services) within certain business entity with discount. Important to note: discount is provided at the time of purchase. The accounting standard, appropriate to this transaction, is IAS 18 'Revenue', superseded by IFRS 15 'Revenue from Contract with Customers' – both specifying that revenue has to be presented net of discounts.

Accounting of such sales comes easy for bookkeepers: in this case the sales discounts

account appears in the income statement and is a contra revenue account, which means that it offsets gross sales, resulting in a smaller net sales figure. The presentation of a sales discount (price of an item – \$100, discount – 1%) in the income statement is:

Gross sales	\$100,00
Less: sales discounts	(1,00)
Net sales	\$99,00

A seller may choose to simply present its net sales in its income statement, rather than breaking out the gross sales and sales discounts separately. This is most common when the sales discount amount is so small (as a rule – from 1% to 3%) that separate presentation does not provide material information.

At present there are two types of discount programs: simple and tier-based.

With a *simple* program customers are always awarded with the same level of discount. A tiered program starts with a certain purchase(s) that provide customer with a right to a certain level of discount (in bonus program – allows customers to earn rewards) with every purchase. Tier programs are like video games. Once you complete one level of spending, customers can unlock a new level that gives them access to more significant benefits and more perks [5].

With tiered discount programs the order of discounting does not change – it is the numbers that undergo the change. For the second tier (discount 2%) the income statement will be the following:

Gross sales	\$100,00
Less: sales discounts	(2,00)
Net sales	\$98,00

Tiered programs motivates customers in lower tiers to make an effort to get to the next level of spending, giving the best rewards to the most loyal customers. The more exclusive the reward, the greater the appeal to customer. At present such program is running in Megamarket network (ultimate discount – 4%).

Depending on the type of agreement with an acquiring bank in some cases, from the point of bookkeeper, *cashback CLP* are the same as discount CLP (in relation to the seller). Here the buyer receives discount in cash form while the seller is recording discounted price.

But by and large, in a cashback transaction it is the credit card company that is sharing a portion of the transaction fee, generated from the merchant, with the consumer in order to incentivize consumers to use their credit card (which generates fees for the company). The amount of a cash-back reward can range from 1% to 20% of a transaction. Credit cards often offer varying cash-back levels, depending on the type of purchase. For example, a cardholder might

earn 3% back on groceries, 2% on stationary purchases, and 1% on all other purchases. Some card companies let cash rewards be used toward specific purchases, including entertainment, electronics, or partnership programs. Thus, it is possible to differ Flat rate, Tiered rate and Different rate Cashback programs.

In this scenario the seller receives (and records) all-in-price.

At present cashback program is run by PrivatBank: cardholders are entitled to receive up to 20% of the price of bought item on their accounts.

Alongside with discount programs many Customer loyalty programs are based on the system of *bonuses*. While clients as a rule do not pay attention to the difference between discount and bonus, in accounting these two objects are implicitly distinct. While discounts are price reductions, the bonuses are rewards: discounts being granted by the seller whilst bonuses are earned by the customer, being a kind of reward for purchasing behavior of the customer, spurring the customer to buy specific commodities more. Also, bonuses differ from discount by:

- time of their provision (bonuses are provided prior to their usage);
- certainty of their usage (bonuses being an option to choose);
- differentiation of the revenues of the parties of multipartite CLP;
- price of the sold items in accounting.

When reward in the Customer loyalty programs is shaped into bonus it means that the client will get a gift or a discount on future purchases from this business entity or its partner. Let's say that a customer, paying the whole price of an item (\$100) receives discount for the purchase of the similar item in future with a discount of 5%. When this occurs an accountant should decide whether to record sales revenue of full \$100 and ignore the future discount, or there should be some impact of the loyalty points on the amount of revenue recognition? Should a bookkeeper treat \$100 as consisting of two parts: a part related to the purchase price of product bought and a part that is a kind of prepayment for future good? Do the bonuses possess real-world monetary value?

To solve these problems the International Financial Reporting Standards Foundation and the International Accounting Standards Board are developing standardized way of recording the sellers' financial performance.

In 2007 International Financial Reporting Interpretations Committee issued IFRIC 13 'Customer Loyalty Programmes'. According to this document

(addressing accounting by entities that grant bonuses / loyalty award credits to customers who buy other goods or services, and problems of accounting for the obligation to provide free or discounted goods or services to customers who redeem award credits), the order of bonuses accounting should be the following:

- An entity that grants bonuses has to allocate some of the proceeds of the initial sale to the award credits as a liability (its obligation to provide the awards). In effect, the award is accounted for as a separate component of the sale transaction.

- The amount of proceeds allocated to the award credits is measured by reference to their fair value, that is, the amount for which the award credits could have been sold separately.

- The entity shall recognise the deferred portion of the proceeds as revenue only when it has fulfilled its obligations. It may fulfil its obligations either by supplying the awards itself or by engaging (and paying) a third party to do so [6].

IFRIC 13 suggested the following order of fair value determination: "the amount for which the award credits could be sold separately". In practice, this definition required significant estimation and judgment by management, which is not a very soft job. That is why in May 2011 International Accounting Standards Board issued IFRS 13 'Fair Value Measurement'.

The valuation techniques, proposed by IFRS 13, is to be based on the following approaches:

- market approach – using prices and other relevant information generated by market transactions involving identical or comparable (similar) assets, liabilities, or a group of assets and liabilities (e.g., a business);

- cost approach – reflects the amount that would be required currently to replace the service capacity of an asset (current replacement cost);

- income approach – converts future amounts (cash flows or income and expenses) to a single current (discounted) amount, reflecting current market expectations about those future amounts [7].

The objective of fair value measurement is to estimate the price at which an orderly transaction to sell an asset or to transfer a liability would take place between market participants at the measurement date under current market conditions (i.e. to estimate an exit price). While using relative fair value method the amount allocated to the bonuses is a proportion of the total consideration based on the fair value of the bonuses relative to the fair value of the initial transaction.

In our example (purchase of an item at \$100 with a bonus of 5%) the consideration to

be allocated is \$100. Fair value of the initial transaction is \$100. Hence the total of the fair values is \$105. According to the relative fair value method, the consideration would be apportioned as follows:

Initial transaction	\$95,24	$(\$100 : \$105) \times \$100$
Bonus	\$4,76	$(\$5 : \$105) \times \$100$
Total	\$100,00	
Thus, the bookkeeper should account:		
Debit	Cash	\$100
Credit	Revenue	\$95,24
Credit	Deferred income	\$4,76

In the ensuing years both the IASB and the FASB had to acknowledge that existing disclosure requirements were unsatisfactory, as they often resulted in information being disclosed that was not sufficient for users of financial statements to understand the sources of revenue, and the key judgements and estimates that had been made in its recognition. "The information disclosed was also often 'boilerplate' and uninformative in nature" [8].

Thus, in January 2018 IFRIC 13 'Customer Loyalty Programmes' was superseded by IFRS 15 'Revenue from contracts with customers' [9].

The application of the core principle in IFRS 15 has to be carried out in five steps:

- 1) identify the contract(s) with the customer for accounting purposes;
- 2) identify its separate 'performance obligations';
- 3) determine the transaction price of each contract identified for accounting purposes in step 1.
- 4) allocate that transaction price to each of the performance obligations identified in step 2.
- 5) Recognize revenue as or when each performance obligation is satisfied.

The new standard instead of bonuses / loyalty award credits employed definition 'points', and introduced for CLP the new glossary item '*material right*' – that is a right that gives the customer an option to acquire an additional good or service at a price that is lower than its *stand-alone selling price (SSP)*. Important caveat: the customer would not receive this right without entering into the initial sale contract.

If a sale contract awards the customer with some bonuses that constitute a material right, stand-alone selling price of the loyalty points has to be estimated. This estimation should be based on the benefit given through bonus along with allowances made for the probability of customer exercising his/her option to acquire some item at a discounted price. Based on the stand-alone selling prices of bonuses / points and the main product, sale price of the contract is allocated between the sale of the product and points.

The sum allocated to the sale of main item is recorded as revenue at the time of sale, whereas the portion of bonuses is recorded as a contract liability (in other words – a kind of advance payment from customer). In future, when such contract liability is settled, corresponding revenue is recorded either when the customer uses his/her bonuses, or the these bonuses expire.

In our example (purchase of an item at \$100 with a bonus of 5%) transaction price needs to be allocated on the following:

- Sale of products (revenue)
- Bonuses (contract liability)

Based on the historical trends, the company expects that 90% of these bonuses will be redeemed by customers and remaining 10% will expire, therefore the SSP of one bonus is \$0.9 (\$1 x 90% redemption likelihood). Bonuses can be redeemed by the end of the year following the year of their issuance. So, the stand-alone price of one bonus can be calculated as follows:

$$\text{Stand-alone price of one bonus} = \$1 \times 90\% = \$0.9$$

$$\text{Stand-alone price of 5 bonuses} = \$0.9 \times 5 \text{ bonuses} = \$4.5$$

Total transaction price of \$100 is to be allocated between products sold and bonuses awarded as follows:

For the product sold: SSP = \$100,

- Relative % = \$100 / \$100 + \$4.5 = 96%;
- Allocated price = \$100 x 96% = \$96

For the bonuses:

- Relative % = \$4.5 / \$100 + \$4.5 = 4%;
- Allocated price = \$100 x 4% = \$4

The entry made at the time of purchase are as follows:

Debit	Cash	\$100
Credit	Revenue	\$96
Credit	Contract liability	\$4

It must be borne in mind that the cost of products given to customers in exchange for loyalty points is recognised as a revenue expense in P/L.

On delivery of a product to the customer, the seller recognises \$96 of revenue (and cost of product is recognised as a revenue expense in

P/L). The remaining \$4 is presented as contract liability.

Nowadays one can see a great variety of Customer loyalty programmes, based on bonuses provision. They can be labelled as 'Points program', 'Spend-based program', 'Gaming program', 'Free perks program', 'Community program', 'Refer a friend program', 'Omni-channel loyalty programs' etc. In spite of a fundamental difference in the form of awards, in the majority of jurisdictions accounting of the award, provided in the course of their operation, is based on the principles set out in IFRS 15 'Revenue from contracts with customers'.

The significance the changes in the approach to bonuses' accounting can be substantiated by their real-world monetary value volume: as of 2019 in the USA alone, there were an estimated \$48 billion in loyalty currency [10].

**Conclusion.** The corporate financial reporting framework in Ukraine is governed by the requirements outlined in the Law on Accounting and Financial Reporting in Ukraine, which was amended in 2011 with the requirement of the application of IFRS. Part 2 of Article 12 of the Law № 996-XIV provides a list of enterprises for which the application of IFRS is mandatory. They are: enterprises of public interest, large enterprises, public joint-stock companies, enterprises engaged in the extraction of minerals of national importance and enterprises engaged in economic activity by types, the list of which is determined by the Cabinet of Ministers of Ukraine. For today commercial companies are not included in this list. Hereat the sellers continue to interpret bonuses as marketing expenses. Such approach simplifies bookkeeping, but disclosed information is not sufficient for users of financial statements and obstructs detecting the sources of revenue. It is high time for Ukrainian accountants to switch to International Financial Reporting Standards and specifically to IFRS 15 that establishes the principles of reporting information about the nature, amount, timing and uncertainty of revenue and cash flows from a contract with a customer.

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