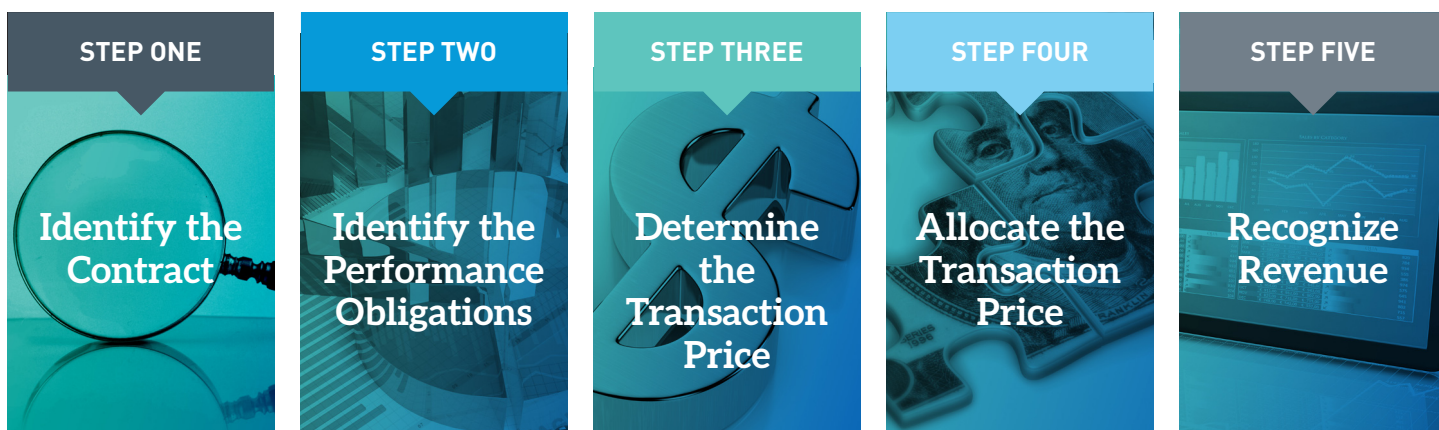




THE NEW REVENUE RECOGNITION ACCOUNTING: WHAT WILL YOUR IMPACT BE?

The impact of ASC 606 (Revenue from Contracts with Customers) affects virtually all industries and public, private and not-for-profit entities who enter into contracts with customers. The far-reaching revenue recognition framework will impact not only a company's accounting but financial reporting, systems, processes, internal controls, financial ratios and contracts.



Implementing the new revenue recognition accounting (ASC 606) is imminent. All private entities must adopt it for fiscal years beginning after December 15, 2018 (ie. January 1, 2019 for calendar year-ends).

Use this high-level assessment tool to assess whether your ASC 606 impact will be minimal, moderate or significant, and identify areas with more complexity. User guide: consider distinct revenue streams; pay closer attention to large, customized arrangements; and bunch generic transactions and evaluate as a group.

We've **bolded** the most sensitive and complex accounting judgements for you.

STEP ONE

1 Identify the Contract

- ☐ For “contract”, think arrangement, purchase orders, formal contracts, etc. May be oral, written or implied by your business practices.
- ☐ The customer agreement must have all necessary approvals. It must identify any/all legally enforceable rights, obligations, and payment terms.
- ☐ Not all **master contracts** are ASC 606 “contracts.”
- ☐ Consider generic vs. **customized agreements**. Custom arrangements will require individual analysis; generic arrangements will not.
- ☐ Agreements with **unilateral termination clauses** are not ASC 606 revenue contracts.
- ☐ Do not move to Step 2 unless an ASC 606 “contract” exists.

STEP TWO

2 Identify the performance obligations

- ☐ Begin by listing all of the goods or services you have promised to your customers.
- ☐ Next, consider your list from the customer’s perspective. Are all of the goods or services your customer ultimately expects to receive on the list? Add/subtract as needed.
- ☐ Last, determine which promises are ASC 606 performance obligations:
 - A promise is a separate performance obligation if it is “**distinct**.” “Distinct” is very similar to the current concept of a deliverable with standalone value to the customer. **Highly interdependent or integrated deliverables** are usually not “distinct” for ASC 606.
 - Disregard any promised goods or services that are immaterial at the contract level.
 - **Customer options for additional goods/services (for free or at a discount)** are usually a separate performance obligation.
 - Shipping and handling is usually not a separate performance obligation
 - Warranties that ensure that the product or service functions as intended are usually not a separate performance obligation.
 - **Installation, customization, training and customer support** are usually separate performance obligations from the primary good or service (if material).
 - **Consult specialized guidance for licenses and royalties.**
- ☐ This step is the **most critical part** of your assessment.
- ☐ Do not move to Step 3 until you know how many and what performance obligations there are.

STEP THREE



3 Determine the transaction price

- ☐ Approach this step at the contract level.
- ☐ Start with the fixed price stated in the contract.
- ☐ Include **good-quality estimates of probable variable consideration** (both positive and negative), such as bonuses, incentives, rebates, discounts, contingencies, etc.
- ☐ Do not include sales tax or bad debts expense.
- ☐ Do not move to Step 4 until you quantify the total transaction price.

STEP FOUR



4 Allocate the transaction price to the performance obligations

- ☐ Skip to Step 5 if there is only one performance obligation.
- ☐ Allocate Step 3's total transaction price amongst the performance obligations (from Step 2) based on **relative standalone selling prices**.
 - ☐ **You may use reasonable estimates** in the allocation process if quoted prices are not available.
- ☐ **Variable consideration may be allocated entirely to one performance obligation if it relates specifically to it.**

STEP FIVE



5 Recognize revenue for each performance obligation

- ☐ Recognize revenue when (at a point in time) or as (over time) the customer obtains control of the good or service.
- ☐ Recognize allocated revenue (from Step 4) separately as each performance obligation is satisfied.
- ☐ **Consult specialized guidance for licenses and royalties.**



AREAS WITH SPECIAL CONSIDERATIONS:

- Franchisors
- Income Taxes
- Recording Revenue at Gross or Net
- Contract Modifications
- Expanded Disclosure Requirements
- Reward, Loyalty or Incentive Programs
- Long-term Contracts
- Long-term Financing Terms (both Explicit and Implicit)
- Nonrefundable Payments
- Potential Restatements of Prior Years' Financial Statements
- Impact on Sales Commission Plans and Financial Reporting
- Impact on Internal Controls, General Ledger and IT Systems
- Upfront Costs to Fulfill a Contract

If your ASC 606 impact will be moderate to significant, we recommend a deeper dive, sooner rather than later. Please contact a Withum professional to guide you through these changing rules.

The information presented in this publication is not necessarily all inclusive, does not constitute accounting, legal, tax or any other advice and should not be relied upon without first consulting with appropriate qualified professionals for your individual business facts and circumstances.



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