ABDO EICK & MEYERS LLP

Certified Public Accountants & Consultants

Quick Reference Guide

Accounting Standard Update 2014-09

"Revenue from Contracts with Customers"

Why do I need this Quick Reference Guide?

As you may know, the Financial Accounting Standards Board routinely releases new accounting standards. Trying to determine how each of these will impact your organization can be a frustrating challenge, to say the least. The release of this particular update, Accounting Standard Update 2014-09, is significant because it amends generally accepted accounting principles—and it could dramatically alter the way you do business.

To help you better understand ASU 2014-09 and the changes it will trigger, we've assembled this Quick Reference Guide. We hope you find it helpful as you prepare for the year ahead. As always, we're here to answer any questions you may have.

Facts about ASU 2014-09

- Issued in 2014 to address the need to converge IFRS® and U.S. GAAP revenue recognition standards into one consistent, comprehensive framework that dictates how much and when revenue should be recognized.
- Supersedes nearly all revenue recognition guidance that currently exists.
- Primarily affects the timing of revenue recognition while increasing disclosure requirements. Requires revenue to be recognized based on performance obligations using a 5-step model.
- Business owners should expect impacts to customer billing, customer contracts, debt covenant calculations, income taxes, and other revenue-based arrangements (such as performance bonuses, sales based commissions, etc.).

When does it take effect?

- **Publicly owned entities:** Fiscal years beginning after Dec. 15, 2017 (2018 calendar year reporting)
- **Privately owned and nonprofit entities:** Fiscal years beginning after Dec. 15, 2018 (2019 calendar year reporting)

Which industries will be affected?

- Virtually all industries in U.S. GAAP, including those that previously followed industry-specific guidance such as the real estate, construction and software industries.

How will it impact my day-to-day activities?

- Revenue must be recognized to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the vendor expects to be entitled in exchange for those goods or services.

This must be done using a 5-step model:

1) Identify the contract(s) with the customer.
2) Separate the contract into "performance obligations."
3) Determine the transaction price of the entire contract.
4) Allocate the transaction price among the different performance obligations that you identified.
5) Recognize revenue as or when each performance obligation is satisfied.

- For certain arrangements, the impact could be a change in timing of revenue recognition, income statement presentation, disclosures, or a combination of all three. The American Institute of Certified Public Accountants (AICPA) has created task forces to address implementation issues and provide guidance for specific industries. Additional information is provided below.

Prepare for these accounting impacts

- Changes in revenue recognition from current accounting:
  - Current revenue recognition under U.S. GAAP is often specific to an industry or transaction.
  - Under new standard, revenue will be recognized based on performance obligations using 5-step model.
  - Expect potential changes in timing and amount of recognition related to contracts with variable consideration (discounts, rebates, incentives, etc.).
  - New criteria to meet collectability requirement may impact amount of revenue recognized.
  - Expect change in recognition and consideration of time value of money for contracts with significant financing components.
  - Transaction price, discounts, and other variable consideration components must be allocated to separate performance obligations.
  - Revenue is recognized when customer obtains *control* of good or service.
    - Control represents ability to direct the use of and receive the benefits from a good or service.

- Changes in disclosure requirements:
  - New standard introduces significantly enhanced overall disclosure requirements for revenue recognition.
    - Even if timing and pattern of revenue recognition does not change, it is possible that new and/or modified processes will be needed in order to comply with the expanded disclosure requirements.
  - Objective is to disclose sufficient information to enable financial statements users to understand nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers.
  - Quantitative and qualitative disclosures for nonpublic entities must include information regarding contracts with customers, significant judgments used, and any assets recognized from costs to obtain or fulfill the contract.

Next steps

- Complying with ASU 2014-09 will require you to review existing contracts, business models, company practices, and accounting policies. Here are a six steps you should take as soon as possible:

  1) Identify revenue streams and determine if they are in scope of the new standard
  2) Review current policies and practices, and identify differences under the new standard
  3) Map policy differences to processes and systems
  4) Educate and communicate within the organization and to users of the financial statements
  5) Consider process and system changes
  6) Draft applicable disclosures

Industry-specific resources

- AICPA task forces have identified several industry-specific considerations and potential issues relating to implementation. We have summarized these below. For a comprehensive list of industries and implementation issues, please visit www.aicpa.org/revenuerecognition.

  Engineering & Construction Contractors

  - Variable consideration/estimation method (including claims, change orders, incentives, penalties, liquidated damages, collectability)
  - Identifying the unit of account (including combining contracts, loss of segmentation guidance, options, and separate performance obligations)
  - Contract costs including pre-contract costs and costs that qualify for capitalization
  - Acceptable measures of progress for contracts that are satisfied over time

  Hospitality

  - Hotel management service arrangements
  - Owned and leased property revenues

  Depository Institutions

  - Service and transaction fees on depository accounts
  - Mortgage servicing or subservicing arrangements not accounted for under ASC 860
  - Sale of non-operating assets (other real estate owned)

  Nonprofit

  - Tuition and housing revenue
  - Subscriptions and membership dues

  Software

  - Determining whether software intellectual property is distinct in cloud computing arrangements

- Identification and satisfaction of performance obligations
- Accounting for a customer’s option to purchase or use additional copies of software
- Defining and identifying potential price concessions
- Estimating the standalone selling price of options that are determined to be performance obligations
- Determine the transaction price by assessing significance of financing component

Telecommunications

- Accounting for individual contracts with customers versus portfolio accounting
- Identification of separate performance obligations in the contract
- Accounting for contract modifications and costs of obtaining a contract
- Considering the effect of the time value of money
- Determining and allocating the transaction price
- Indirect channel sales (including principal vs. agent)

Questions? We're here to help

We've assembled a task force charged with reviewing each standard and providing guidance for our clients, so please don't hesitate to call if you have questions. We can also help you prepare for whatever transitions need to happen within your business. When it comes to changes of this magnitude, it's never too early to plan ahead.