Revenue Recognition

The Past and The Future

January 24, 2018

Jim Dolinar

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Today's Speaker

Jim Dolinar
Managing Partner – Assurance Professional Practice
Crowe Horwath LLP

Agenda

- A Trip Down Memory Lane

  How did we get here?

- More Than Meets the Eye

  Complexities arising from the five-step process

- Thinking through the Impacts

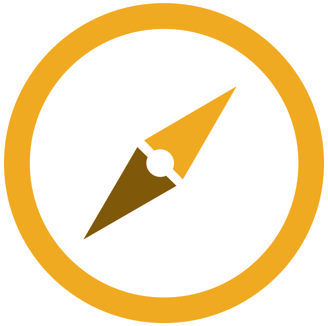
  The *other* effects of ASU 2014-09

- The Future Ahead of Us

  Key observations on the standard and implementation

What Will You Gain From This Session?

As a result of participating in this session, you should be able to:



- Discuss the ASC 606 from a historical perspective
- List key impacts of the new standard
- Describe the five-step model contained in the new revenue recognition standard along with other key concepts and principles
- Identify best practices gleaned from public company implementations.

A Trip Down Memory Lane

A Trip Down Memory Lane – *Where We Were*

International differences

Disclosure shortfalls

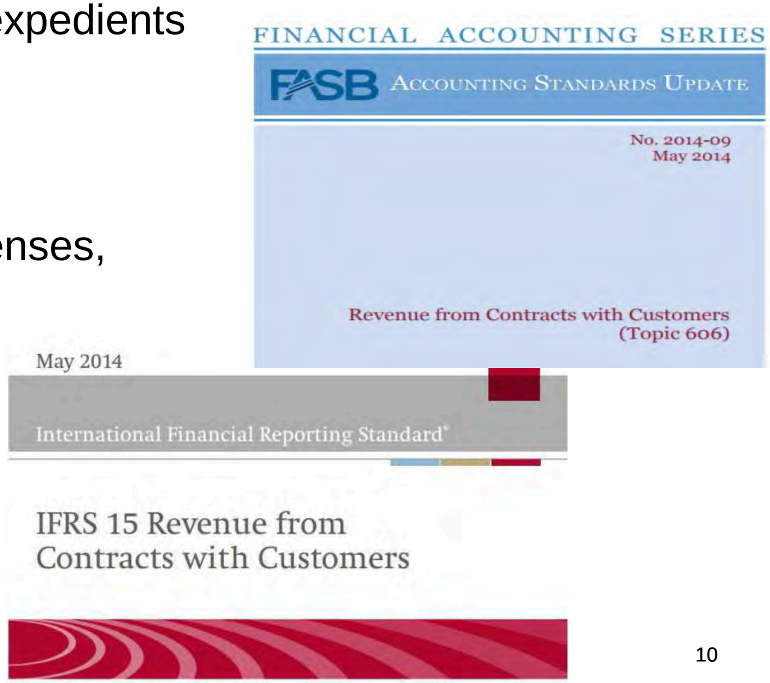
Patchwork guidance

Topic 606 – *Addressing the Existing Shortfalls*

Patchwork guidance	• Grounded on principles (e.g., control, performance obligations) • Bolstered by a five-step framework
Disclosure shortfalls	• Clearly defined disclosure objective • Robust disclosure regimen
International differences	• Topic 606 and IFRS 15 largely converged • IFRS 15 enhances previous international revenue recognition guidance

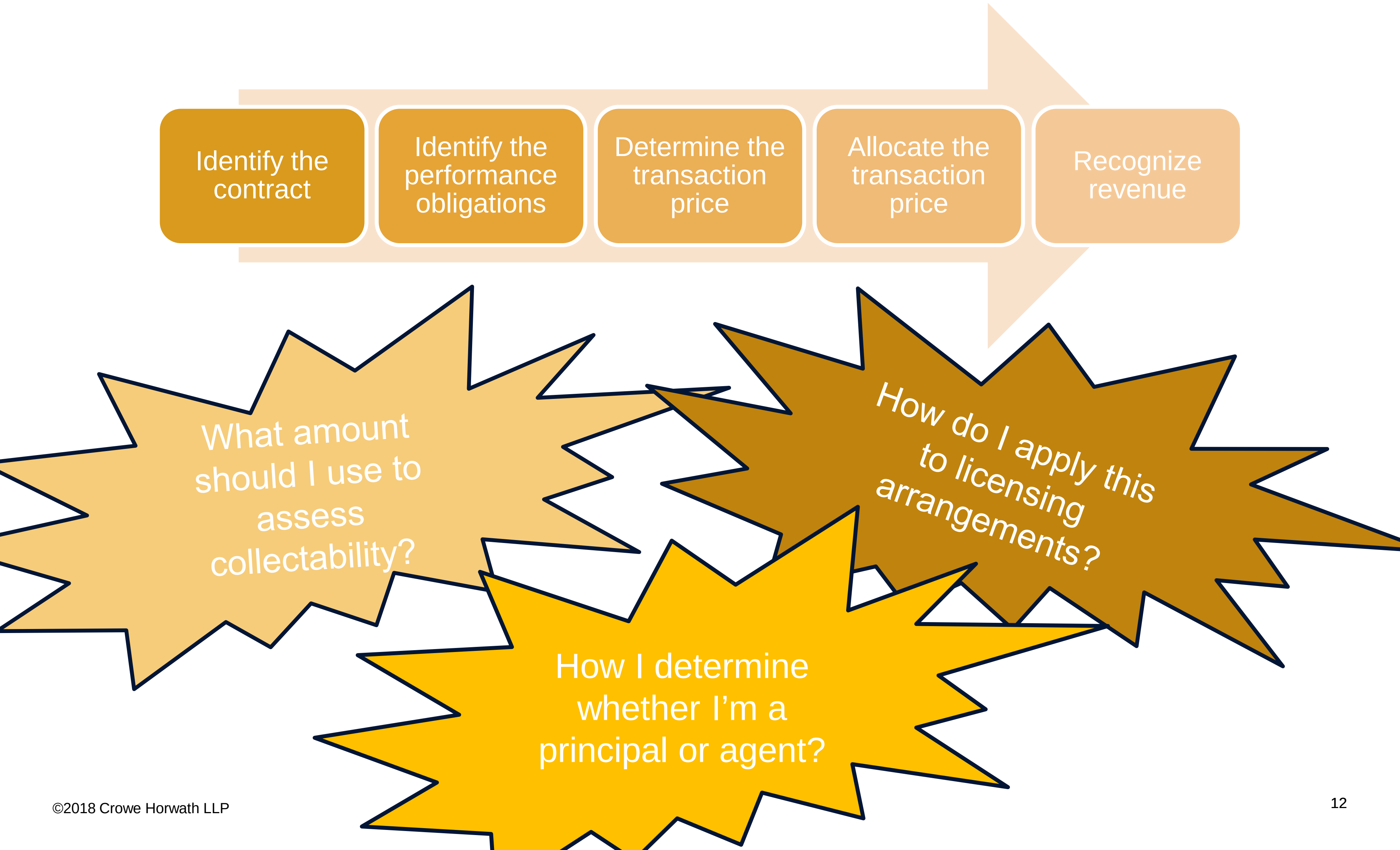
Topic 606 versus IFRS 15 – *Fully Converged?*

- While Topic 606 and IFRS 15 are largely converged, some differences remain
  - Differences in definitions (e.g., meaning of *probable*)
  - Historical conceptual differences (e.g., handling of impairment reversals)
  - Differences in disclosure requirements (e.g., no expedients for “backlog” disclosure)
  - Differences in implementation guidance & practical expedients (e.g., principal vs. agent, licenses, noncash consideration, etc.)



More Than Meets the Eye

More Than Meets the Eye – *Getting Under the Hood*



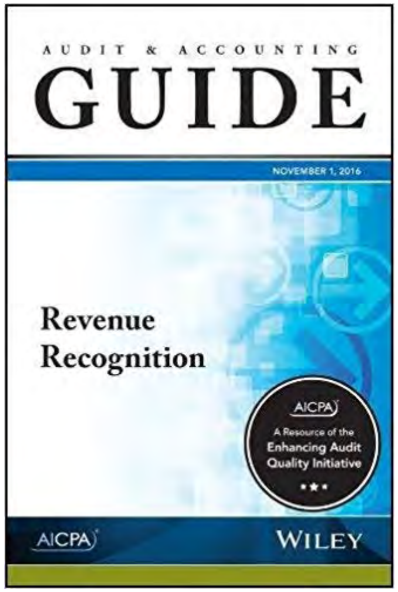
The Revenue Recognition Transition Resource Group (TRG)

- The TRG's objective is to …
  - Solicit, analyze, and discuss stakeholder issues arising from implementation
  - Inform the FASB and the IASB of implementation issues, and offer the standard-setters suggestions on how to address
  - To provide a forum for stakeholders to learn about the new guidance
- Primary results …
  - TRG issue papers
  - ASUs 2016-08, 2016-10, 2016-12, and 2016-20

The AICPA Rev Rec Task Force – *Industry to the Rescue*

- To address industry-specific implementation issues, the AICPA formed 16 industry revenue recognition working groups
- Final issue papers included in new Revenue Recognition Guide
- Current status of work to date:

# of Identified Issues	# of Issues Exposed	# of Issues Finalized
136	123	83



The SEC, Early Adopters, Etc. – *Learning from Others*

- Resources from the SEC and Early Adopter Experience
  - ➢ SEC speeches (e.g., use of "reasonable judgment", principal v. agent)
  - ➢ Early adopter financials … and SEC comment letters
- Also FASB Technical Inquiry Process

Thinking Through the Impacts

Thinking Through the Impacts – *Lest We Forget*

Beyond the top line

Disclosures

ASU 2014-09

Business practices

Processes and controls

Thinking Through the Impacts – *Beyond the Top Line*

- In addition to revenues, ASU 2014-09 also affects:
  - The accounting for contract costs (to obtain and fulfill)
  - Transfers of non-financial assets (e.g., sales of real estate)
  - Lease accounting (e.g., sale-leasebacks, lessor accounting)

Thinking Through the Impacts – *Disclosures*

Enable users of the financial statements to understand the **nature, amount, timing, and uncertainty** of **revenue and cash flows** arising from contracts with customers

- Disaggregation of revenues, by relevant economic factors
- Contract balances
- Performance obligations, including yet-to-be-earned amounts
- Significant judgments, and changes in judgments
- Contract costs

Consider data needs and system impacts

Thinking Through the Impacts – *Business Practices*

- "Customary business practices" may affect:
  - ➢ Existence of distinct performance obligations (e.g., warranties)
  - ➢ Determination of transaction price (e.g., implicit price concessions)

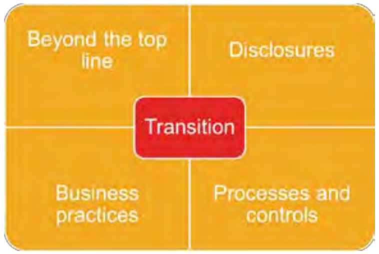
- The impact of ASU 2014-09 could result in changes to:
  - ➢ Compensation plans, other contractual arrangements
  - ➢ Information systems

Thinking Through the Impacts – *Processes and Controls*

Step 1	• Assessing the collectability criteria • Evaluating contract modifications
Step 2	• Evaluating whether customer options are material rights • Identifying distinct performance obligations
Step 3	• Evaluating significant financing components • Constraining variable consideration
Step 4	• Estimating the standalone selling price • Reevaluating the accuracy of judgments and assumptions
Step 5	• Measuring progress towards satisfaction of obligations • Determining whether obligations are point in time vs. over time

Thinking through the Impacts – *Transition Method Choice*

- ASU 2014-09 allows an entity to select one of the following:
  - ➢ Full retrospective method
  - ➢ Modified retrospective method



Full retrospective method		Modified retrospective method	
Pros	***Cons***	***Pros***	***Cons***
• Comparative financial data • Practical expedients to assist with implementation	• Data needs to restate prior periods • May require significant implementation efforts	• Relief from restating prior periods • Completed contracts need not be restated	• Requirement to report revenues under new/old method • Greater likelihood of “losing” revenues at transition

The driving consideration should be the needs of the users of financial statements

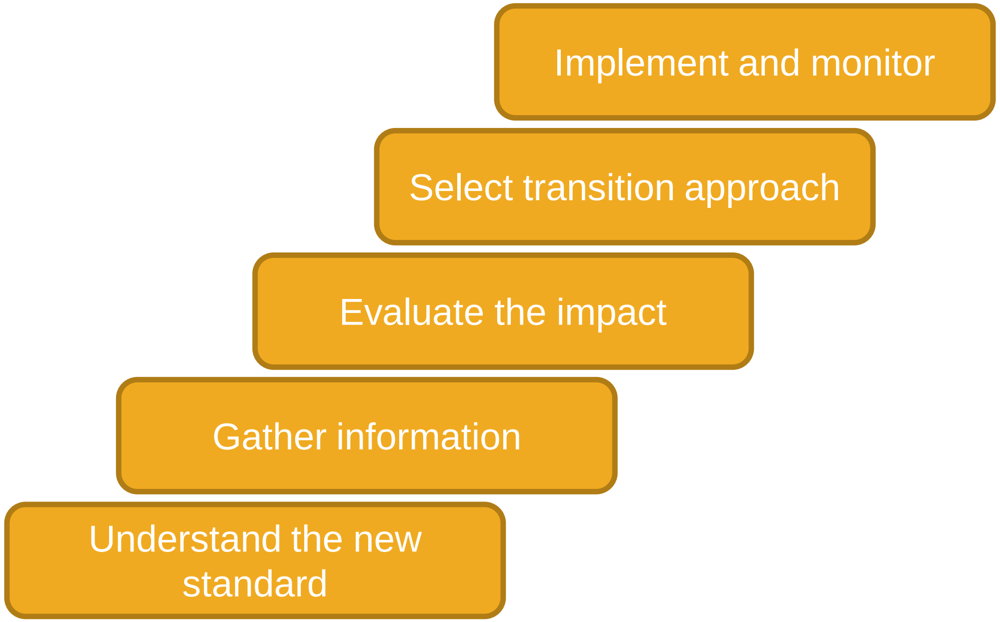
The Future Ahead of Us

Public Company Considerations – *What If…?*

- If you are considering going public, don't forget:
  - Unless determined to be an emerging growth company (EGC), you will need to adopt Topic 606 before going public
  - EGCs may elect to apply private company effective dates; but, may be at a disadvantage to peers who have already adopted
  - ASC 606 could have a significant impact on a company's processes and surrounding controls (SOX implications)
- Other considerations:
  - If a public business entity solely because you include financial statements or financial information in another entity's SEC filing (e.g., significant equity method investee or acquisition), you may adopt ASC 606 using either public company or private company deadlines

The Future Ahead of Us – *Parting Thoughts*

- More to ASU 2014-09 than initially meets the eye
- Take advantage of the guidance and first-mover examples available to you
- Look beyond the top line
- Start early



Thank you

Jim Dolinar
Partner
Assurance Professional Practice
Crowe Horwath LLP

Office 630.574.1649
jim.dolinar@crowehorwath.com

Crowe Horwath.

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Revenue Recognition: The Five Step Process

January 24, 2018

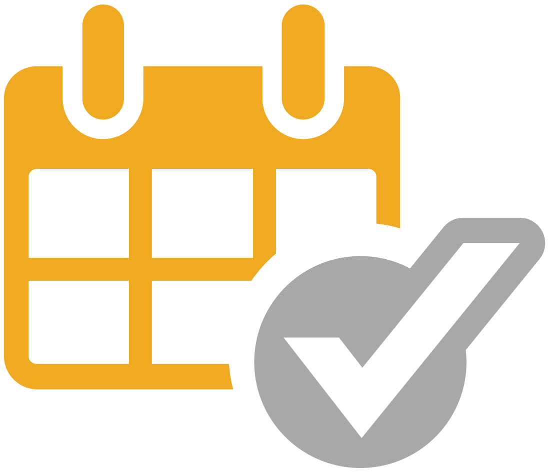
Scott Sachs

Today’s Speaker

Scott Sachs
Partner
Audit Services
Crowe Horwath LLP

Agenda

- Background and Refresh
- Accounting Standards Updates and Specialized Topics
- Presentation and Disclosure
- Key Takeaways from Implementations



Objectives

By participating in this session, you should be able to:

- Identify best practices gleaned from public company implementation of the standard.
- Describe the five-step model contained in the new revenue recognition standard along with other key concepts and principles.

Background and Refresh

Background

- The FASB and the IASB have issued largely converged revenue recognition standards that will supersede virtually all revenue recognition guidance in U.S. GAAP and IFRS.

- The new standards provide accounting guidance for all revenue arising from contracts with customers and affects all entities that enter into contracts to provide goods or services to their customers (unless the contracts are in the scope of other U.S. GAAP or IFRS requirements, such as lease requirements).

- The core principle is that an entity will recognize revenue at an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring goods or services to a customer.

Understand the New Standard

Resources to help you:

- Crowe Horwath LLP Revenue Recognition Resource Center: Includes our guidance along with industry-specific guidance. www.crowehorwath.com/revenue-recognition

- Transition Resources Group for Revenue Recognition (TRG): The TRG was formed by the FASB and IASB to help determine whether more guidance was needed to address implementation questions and to educate constituents. http://www.fasb.org/jsp/FASB/Page/LandingPage&cid=1176164065747

- AICPA Revenue Recognition Task Forces: The AICPA has formed 16 industry task forces to help develop a new Accounting Guide on Revenue Recognition that will provide illustrative examples for how to apply the new revenue recognition standard. www.aicpa.org/InterestAreas/FRC/AccountingFinancialReporting/RevenueRecognition/Pages/RevenueRecognition.aspx.

- The industries involved with this project are:

Aerospace and defense	Gaming	Oil and gas
Airlines	Healthcare	Power and utility
Asset management	Hospitality	Software
Broker-dealers	Insurance	Telecommunications
Construction contractors	Not-for-profit	Timeshare
Depository institutions		

The Five Steps of Revenue Recognition

1. Identify the contract(s) with the customer
2. Identify the performance obligations in the contract
3. Determine the transaction price
4. Allocate the transaction price to the performance obligations
5. Recognize revenue when (or as) the entity satisfies the performance obligations

Effective Dates and Transition Requirements

Effective dates

- Public entities: fiscal years beginning after Dec. 15, 2017, including interim periods within those fiscal years
- Nonpublic entities: fiscal years beginning after Dec. 15, 2018; interim periods beginning after Dec. 15, 2019
- Early application: permitted for all U.S. entities for fiscal years beginning after Dec. 15, 2016, including interim periods within those fiscal years

Transition

- Full retrospective application
- Modified retrospective application

Accounting Standards Updates and Specialized Topics

Accounting Standards Updates and Specialized Topics

The FASB has issued the following ASU to address implementation issues:

- ASU 2016-08 – “Revenue From Contracts With Customers (Topic 606): Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net)”
- ASU 2016-10 – “Revenue From Contracts With Customers (Topic 606): Identifying Performance Obligations and Licensing”
- ASU 2016-12 – “Revenue From Contracts With Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients”
- ASU 2016-20 – “Revenue From Contracts With Customers (Topic 606): Technical Corrections and Improvements”

Specialized Topic - Costs to Obtain a Contract

- Under the new guidance, the incremental costs of obtaining a contract with a customer are recognized as an asset if the entity expects to recover them (less than one year practical expedient provided).

- The incremental costs of obtaining a contract are those costs that an entity incurs to obtain a contract with a customer that it would not have incurred if the contract had not been obtained (for example, a sales commission).

- Once capitalized, the asset shall be amortized on a systematic basis that is consistent with the transfer to the customer of the goods or services to which the asset relates.

- Costs to obtain a contract that would have been incurred regardless of whether the contract was obtained shall be recognized as an expense when incurred, unless those costs are explicitly chargeable to the customer regardless of whether the contract is obtained.

- The new guidance may be a significant change in practice for entities with contract periods greater than one year that historically have expensed the costs of obtaining a contract and now will be required to capitalize them.

Presentation and Disclosure

Presentation of Contract Assets and Contract Liabilities

A contract asset or liability is generated depending on the relationship between the entity's performance and the customer's payment.

- When an entity satisfies a performance obligation by transferring a promised good or service, the entity has earned a right to consideration from the customer.

- If an entity has an unconditional right to receive consideration from the customer, the right is accounted for as a receivable and presented separately from other contract assets. A right is unconditional if nothing other than the passage of time is required before payment of that consideration is due.

- If an entity has a conditional right to receive consideration from the customer, the right is accounted for as a contract asset. The right would be conditional, for example, when an entity first must satisfy another performance obligation in the contract before it is entitled to payment from the customer.

- When the customer performs first (e.g., by prepaying its promised consideration), the entity has a contract liability.

Annual Disclosure Requirements

The objective of the new disclosure requirements in the new standard is for an entity to disclose sufficient information to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows from contracts with customers.

To achieve that objective, an entity is required to disclose qualitative and quantitative information about all of the following:

- Its contracts with customers
- The significant judgments, and changes in the judgments, made in applying the guidance to those contracts
- Any assets recognized from the costs to obtain or fulfill a contract with a customer.

The detailed disclosure requirements of each of these topics differ for public and nonpublic entities.

Key Takeaways From Implementations

Key Takeaways From Implementations

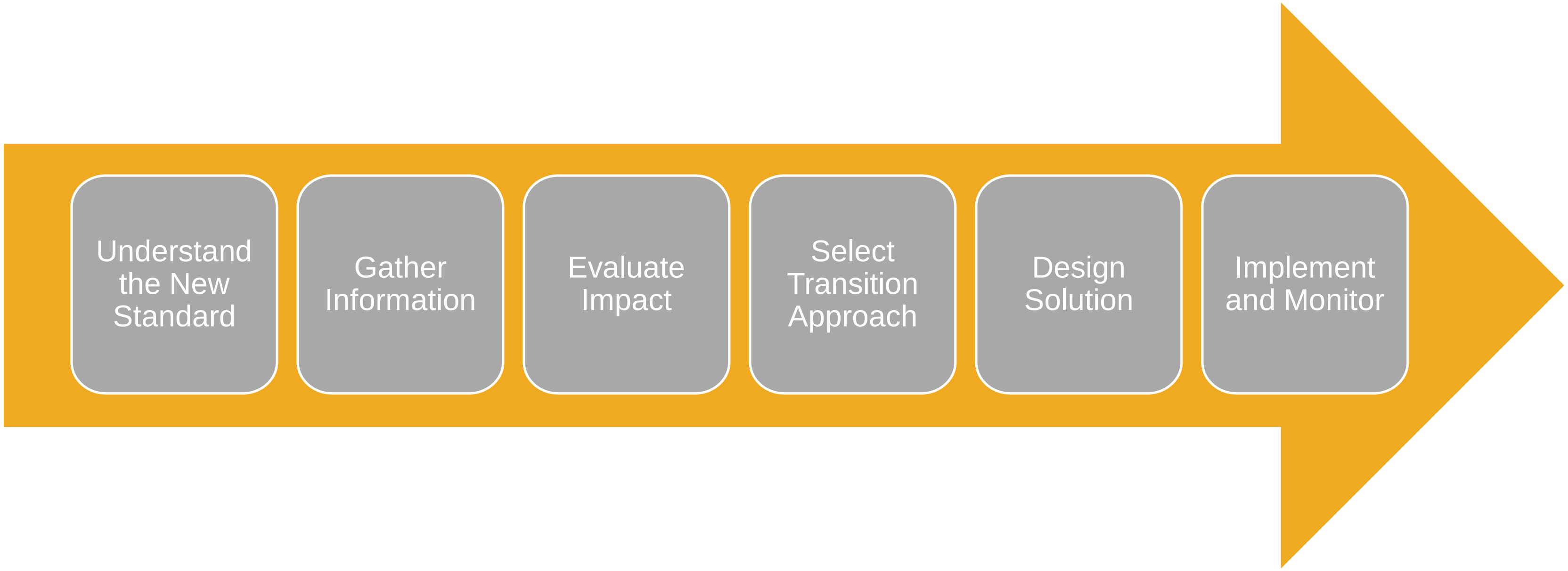
Common challenges to timely implementation of the new revenue recognition standard:

- A lack of time and resources

- Assumption the new revenue recognition standard will have an immaterial effect on the company's financial statements

- Perception the standard is not finished and clarifications are not finalized

Key Takeaways From Implementations



Crowe Horwath.

Thank you

Scott G. Sachs, CPA
Partner, Audit Services
scott.sachs@crowehorwath.com