NDH

Preparing for Change
How to Manage the New Revenue Recognition Standards

CFO Starting Line: Helmsman's View

CFOs prepare to address new standards for revenue recognition, navigating through similar waters, but with new tactics.
Financial performance depends on their hitting the mark.

Topics of Presentation

- Defining the Landscape
- ASC 606: What It Governs and How it Came To Be
- Details of the Revenue Recognition Model
- Subtopics of the Revenue Recognition Model
- Systems for 606: Managing Revenue in the New Economy
- Appendix

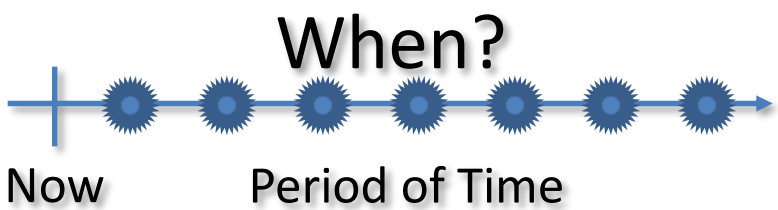
Defining the Landscape

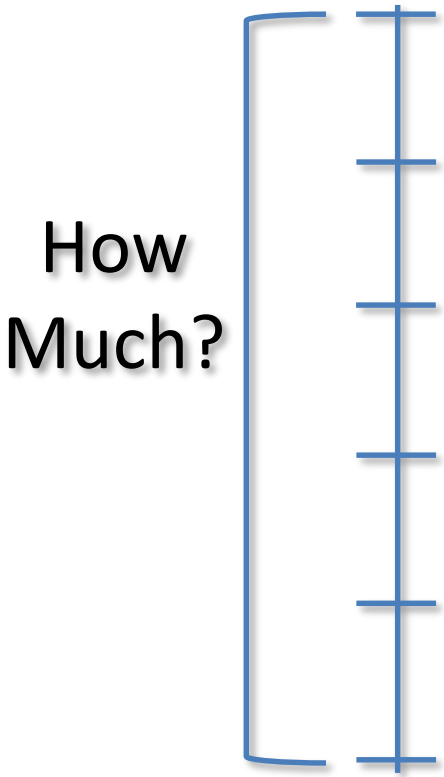
Revenue Recognition: An Ongoing Narrative

As always, accounting for revenue is a consideration of:

When?

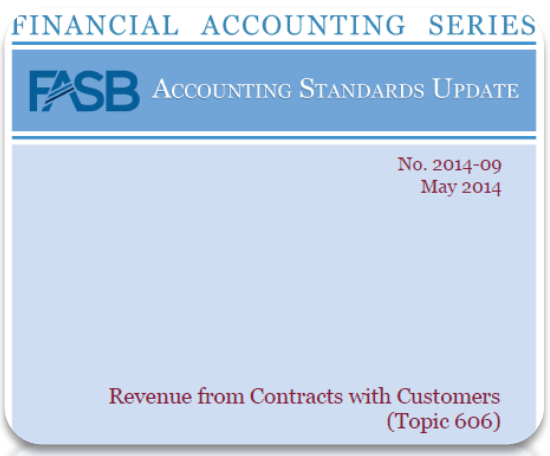
How Much?





ASC 606: Title Focus

For the new rev rec standards the application of
when and *how much*
is specific to *contracts* with *customers.*
FASB's Accounting Standards Update 2014-09,
or Topic 606 is:
Revenue from Contracts with Customers



ASC 606: Content Focus

FASB outlines its *scope* and *focus:*

"The guidance in this Update affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards (for example, insurance contracts or lease contracts)."[1]

ASC 606: Title Focus

FASB defines a *contract* as:

"…an agreement between two or more parties that creates enforceable rights and obligations."[1]

ASC 606: Title Focus

…and a *customer* as:

"A party that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration."[1]

Viz. contracts that relate an entity's operating business, rather contracts with "buyers," which would more naturally apply to non-operating business contracts.

ASC 606: Core Principal

While financial managers look for a new set of rules to abide by, they may miss the *core principal* concerning *performance*, and *entitlement*.

"The core principle of the guidance is that an entity should recognize revenue to depict the transfer of the promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchanges for those goods or services."[1]

ASC 606: Summary

In summary, for entities writing contracts with customers, the narrative of when and how much revenue to recognize must reflect the core principal of *performance* and *entitlement*.

How Does the Core Principal Change Rules?

Legacy Vs. New Standards: How Main Provisions Differ		
Revenue Recognition Topic	**Legacy Standards: ASC 605…**	**New Standard: ASC 606**
When Revenue is Recognized	• When realized or realizable *And…* • When earned[1] Revenue recorded with receipt of cash and delivery	• When each performance obligation (or distinct goods or services) is satisfied.[2] Revenue recorded when the entity performs
	⇨ Difference: receipt of assets and delivery vs. performance	
How Much Revenue is Recognized	**Legal Contract Concept** – Transaction amounts which the entity *contracts* to be entitled, based on *promises* to pay. Allowances recorded, but no variable consideration	**Accounting Contract Concept** – Transaction amounts which the entity *expects* to be entitled, based on *potential* to pay. No allowances recorded, but variable consideration
	⇨ Difference: net vs. gross (consistent with entitlement)	

FASB Five Step Model of Rev Rec Process

FASB provides a five step model of the rev rec process, to help with the ordering of your contracts, and for answering the questions of “when” and “how much.”

An entity recognizes revenue in accordance with the core principle by applying the five steps.

Five Steps of the Revenue Recognition Model

1. Step 1: Identify the contract with the customer
2. Step 2: Separate performance obligations in the contract
3. Step 3: Determine the transaction price which the entity expects to be entitled
4. Step 4: Allocate the transaction price to the individual performance obligations
5. Step 5: Recognize revenue as the entity satisfies the performance obligations

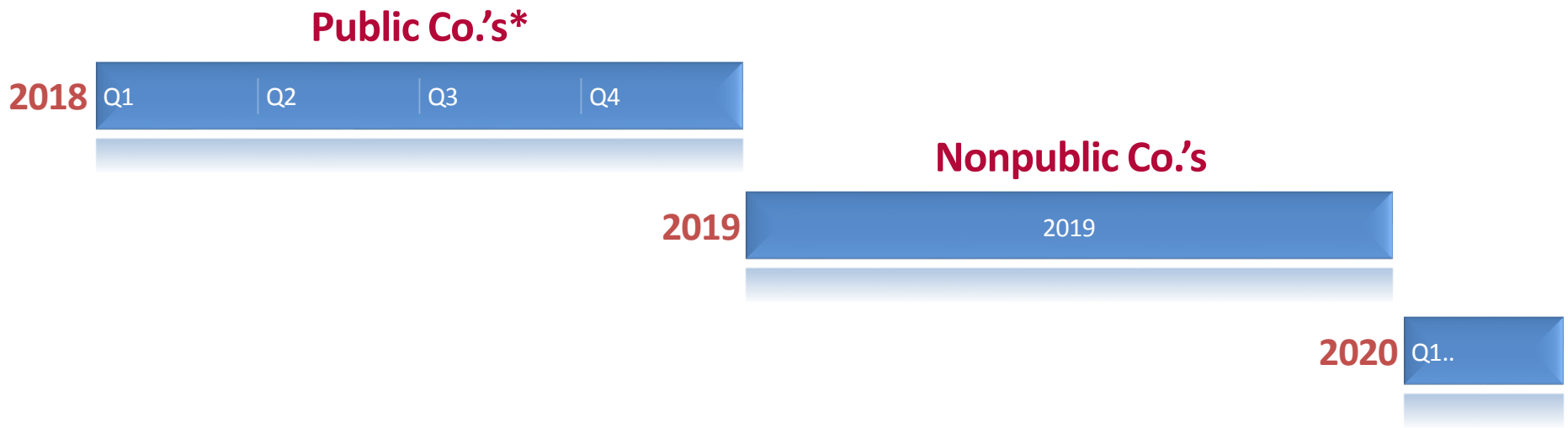
Subtopics of the Revenue Recognition Model

Additional Guidance for ASC 606	
Subtopic	**606 Requirements**
Contract Modifications	If there's a change in price or scope (or both) of the original contract, with both parties agreeing, additional guidance is offered within the overall context of applying ASC 606.
Licensing	If the entity has licensing agreements, which are distinct or predominantly distinct in the contract, refined guidance is offered within the overall context of applying ASC 606.
Costs Related to a Contract	An entity shall recognize as an asset (deferred cost)[1]: • Incremental costs of *obtaining a contract* with a customer • Costs incurred in *fulfilling a contract* with a customer
Presentation	Presentation requirements for contract assets and liabilities, and their respective impact on the statement of activities.
Disclosures	Disclosure requirements for "…the nature, amount, timing, and uncertainty of revenue and cash flows…"[2] • Contract balances by unbilled, billed, and paid

Who and When?

Applies to all entities, with attestation requirements, including nonpublic entities that previously had "tag along" guidance related to rev rec (private, NFP).

Public Co.'s Effective: Annual & interim periods beginning after 12/15/17
Nonpublic Co.'s Effective: Annual beginning after 12/15/18, interim 2020



***Also, NFP (w/Issued Securities), EE Benefit Plans**

Materiality Doesn't Drive Compliance

Materiality <> compliance with the new standards

That is, even if the changes don't materially impact results, audited financials will still need to reflect the new accounting provisions, process, and disclosures.

To wit, early indications show financial effects are varied:

Impact on Opening Balances of Retained Earnings as of 03/31/17 (AuditAnalytics.com)		
Company	**Transition Method**	**Impact on Opening R/E**
Alphabet Inc.	Modified Retrospective	($15,000,000)
UnitedHealth Group Inc	Modified Retrospective	Impact was not material
Ford Motor Co	Modified Retrospective	$36,000,000
Raytheon Co	Full Retrospective	$91,000,000
General Dynamics Corp	Full Retrospective	($684,000,000)

A Global Standard

A joint standard for organizations following US GAAP *and* IFRS

Accounting for Revenue from Contracts with Customers		
Who	**Combining For**	**Version of Joint Standard**
FASB	Single Comprehensive Model (Unified Standard)	ASU 2014-09
IASB		IFRS 15

FASB FINANCIAL ACCOUNTING STANDARDS BOARD

IFRS™

How to Administer 606 & New Economy?

ASC 606 and the new economy demand systems with the architecture to support contracts, and the nuances of subscriptions, complex-pricing, and interconnected business.

To serve CFOs, ERP systems must administer the five steps 606, and manage new economy transactions.

Main Provisions of 606 as Applied to Systems

1. Model: Identify the Contract
   System: Contract Object
2. Model: Separate Performance Obligations
   System: Contract Line Item
3. Model: Determine Transaction Price
   System: Line Item Fixed or Variable Amount
4. Model: Allocate Transaction Price
   System: MEA Price List, Allocation, Reallocation
5. Model: Recognize Revenue
   System: Revenue Templates and Schedules

Managing New Economy Transactions

In addition to changes from ASC 606, mega-trends in the economy are driving how CFOs manage their businesses, and maintain their financial systems to support operations and reporting.

What's In It for the CFO?

Potential advantages of the new revenue standards for CFOs:

- Closer comparability of revenue between Co.'s
- Disclosures prompt enhanced reporting
- Less complex (less industry-specific)
- Harmonization of global standards
- Parity between public and private Co.'s
- Relevance as markets evolve (principal-based)

ASC 606: What It Governs and How it Came To Be

What Governed Will No Longer Govern

"This overhaul supersedes nearly all the revenue recognition guidance that currently exists."[1]

The following standards and will no longer be standard: FASB 5, FASB 6, ASC 605-10, SAB No. 101, 104, etc.

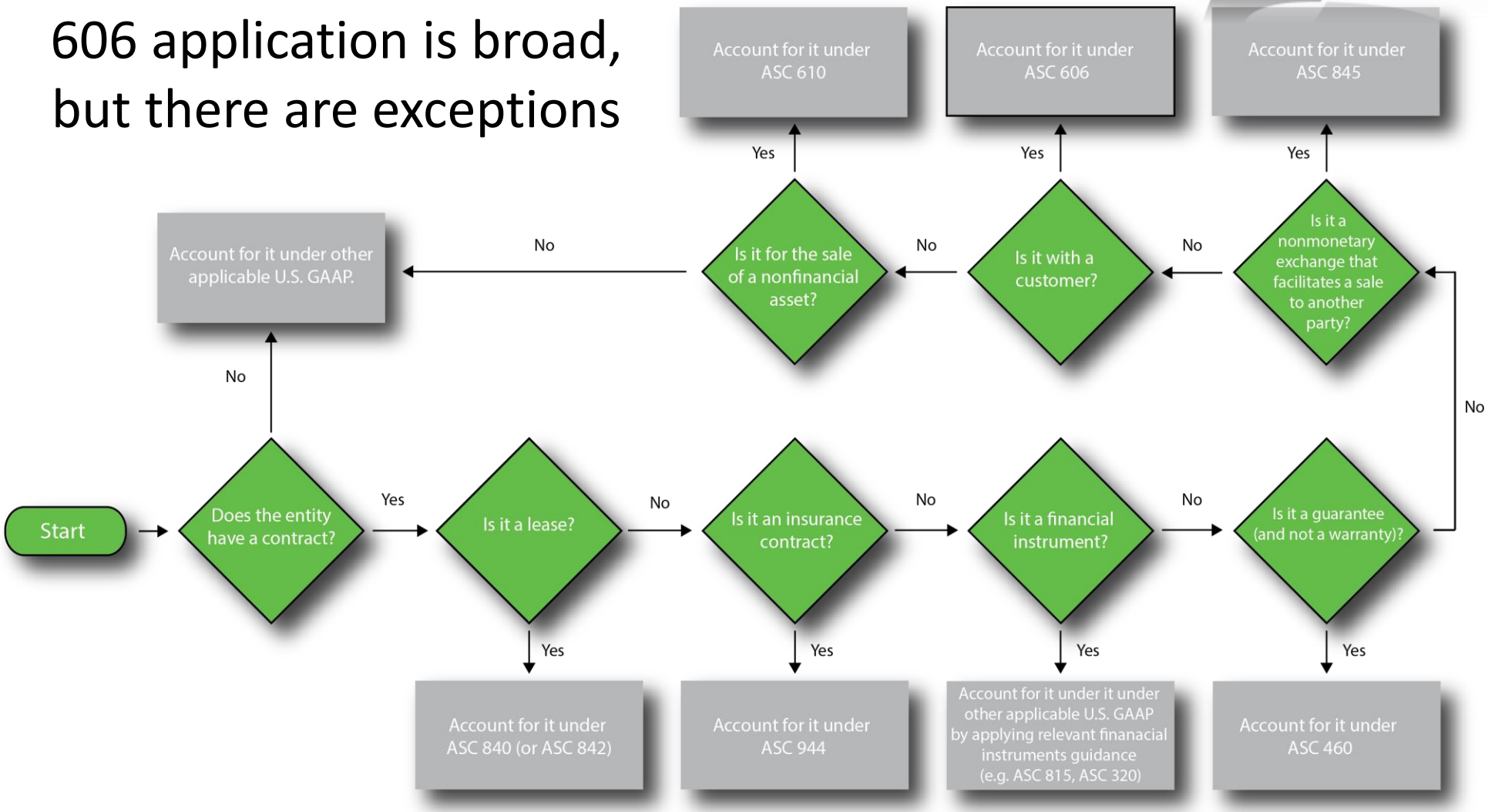
Current Revenue Recognition Guidance

Current Sources of US GAAP Governing Rev Rec (sample):

- **FASB 5** – Issued Dec, 1985 Statement of Financial Accounting Concept (SFAC) No. 5, Recog. & Mea. in Fin. State. of Biz. Enterprises
- **FASB 6** – Issued Dec, 1985 Statement of Financial Accounting Concept No. 6, Elements of Fin. State. (definition of "revenue")
- **ASC 605-10** – Existing US GAAP guidance on revenue recognition – overall; Codification of FASB 5
- **ASU 985-605** – Issued Oct, 2009 Accounting Standards Update 2009-14; Software – Revenue Recognition (Topic 985)
- **SAB No. 101, 104** – Issued 1999, amended 2003; per SEC Re: rev rec for public entities, but private companies practiced by analogy

Account for It Under ASC 606?

606 application is broad, but there are exceptions



Deloitte "A Roadmap to Applying the New Revenue Recognition Standard, 2017," p37

Why FASB and IASB Moved?

Officially, FASB and IASB identified these issues and objectives for the new standard[1]:

1. Remove inconsistencies and weaknesses in revenue requirements.
2. Provide a more robust framework for addressing revenue issues.
3. Improve comparability of revenue recognition practices across entities, industries, jurisdictions, and capital markets.
4. Provide more useful information to users of financial statements through improved disclosure requirements.
5. Simplify the preparation of financial statements by reducing the number of requirements to which an entity must refer.

The AICPA Says "History of Concern"

…and the AICPA identified these issues related to the current rev rec standards (see "history of concern"[1]):

- Longer than expected payment terms
- Installment receivables
- Significant sales recorded at end of reporting period
- Channel stuffing
- Sales prior to delivery of goods "bill-and-hold" "ship-in-place"
- Barter transactions
- Side-agreements
- Sales requiring substantial vendor involvement
- Partial shipments
- Overly optimistic percentage of completion

How Does ASC 606 and Related Differ?

The Transition from Existing to New Standards

Existing Vs. New Standards: How Main Provisions Differ		
Revenue Recognition Topic	**Existing Standard: FASB 5…**	**New Standard: ASC 606**
Framework	Numerous industry and transaction-specific standards (subtopics of FASB 5).	Largely principles-based; applies to all contracts regardless of industry or transaction.
Source of Guidance	Multiple sources of guidance 1) Industry, 2) general guidance, 3) other sources (EG SEC)	Single source for guidance
Disclosures	Broad, unspecific, aimed at general risk disclosure Re: customer, geographic, product	Specific to nature, timing, and uncertainty of revenue (improve understandability).
Address of Prior Unaddressed	Transactions not addressed dealt with by "implication," or closest reasonable standard, precedent.	Certain transaction specific: 1) Service revenue, 2) contract modification, 3) IP licensing
Application	Applies to public entities, but then practiced by analogy by private Co.'s.	Applies to all entities • Public • Non-public: Private, NFP

How the New Rev Rec Standard Came To Be

FASB and IASB Revenue Recognition Project Timeline: Standard and Amendments		
ASU, IFRS	**Date**	**Guidance**
ASU 2014-09 IFRS 15	May, 2014	Final standard on revenue recognition issued
ASU 2015-14	August, 2015	Change in the effective date of implementation for ASC 606 for both public, and non-public companies
ASU 2016-08	March, 2016	Principal versus agent considerations (reporting revenue gross versus net)
ASU 2016-10	April, 2016	Identifying performance obligations ("separately identifiable") and licensing (IP considerations)
ASU 2016-12	May, 2016	Narrow-scope improvements, practical expedients (collectability, presentation of sales tax, non-cash)
ASU 2016-20	December, 2016	Technical corrections for impairment testing, disclosures, contract modifications, and others
--	2017	Early adoption election for public and non-public Co.'s

Accounting Guidance for Industry Groups

The AICPA formed 16 industry task forces to help develop accounting guidance for the new rev rec standard

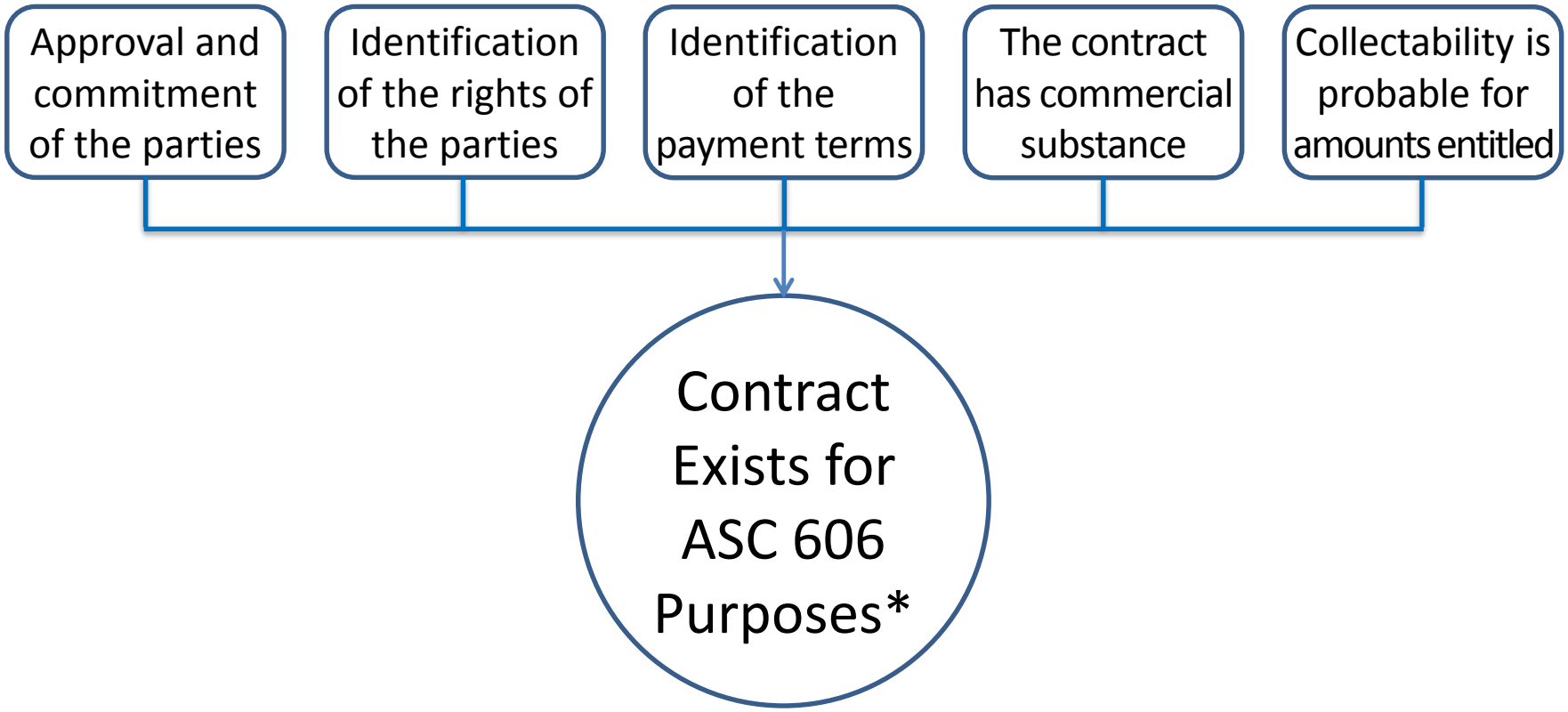
Industry Task Forces			
	Aerospace & Defense		Hospitality
	Airlines		Insurance
	Asset Management		Not-for-Profit
	Broker Dealers		Oil & Gas
	Engineering & Construction		Power Utility
	Depository Institutions		Software
	Gaming		Telecommunications
	Healthcare		Timeshare

Details of the Revenue Recognition Model

Details of the Revenue Recognition Model

1 Identify the Contract(s) With the Customer

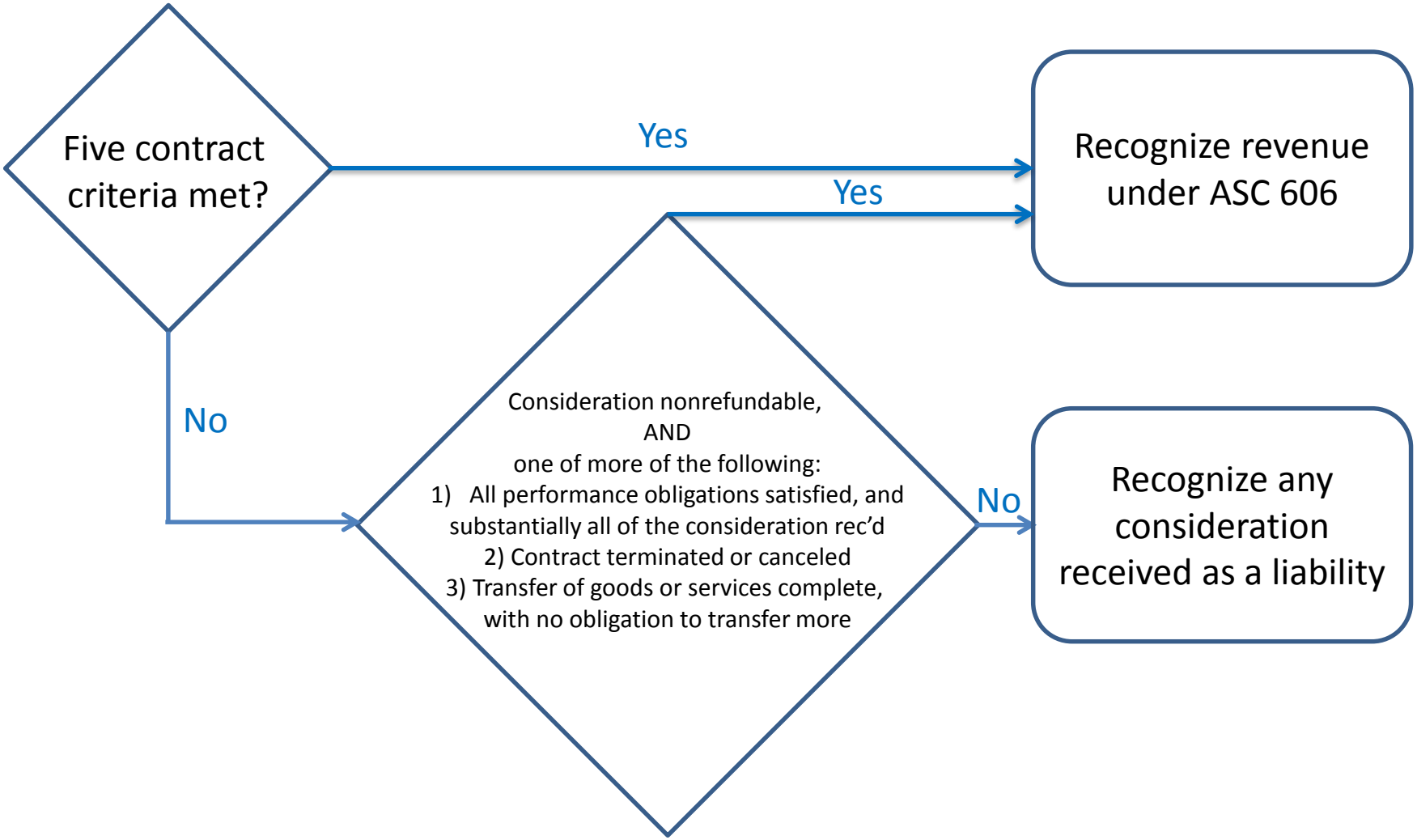
Step 1: Given these contract criteria, ASC 606 applies



*If *any* of the above 5 contract criteria are not met, the ASC 606 rev rec model cannot be applied

Details of Step 1 of the Rev Rec Model

Recognize as revenue or treat consideration as a liability?



Details of Step 1 of the Rev Rec Model

Point of Clarification

Termination – A contract is considered terminated if:

- The customer has no further rights to good or services
- The entity has no further intention of delivery

⇨ In this case, revenue can be recognized to the extent of nonrefundable consideration received (that is, now, or at the point-in-time when termination is assessed).

⇨ This is the case, even if the entity pursues collection of outstanding balances from the customer.

Details of Step 1 of the Rev Rec Model

Combining – At contract inception, multiple contracts should be considered for combination into a single arrangement with the customer; one of the three following conditions require a combination of contracts:

- The contracts are negotiated as a package, with a single commercial objective.
- Amount paid in one contract depends on the price or performance of the other contract.
- The goods or services in the contract are a single performance obligation.

Details of Step 1 of the Rev Rec Model

Existing Vs. New Standards: Recognizing Revenue When Cash is Received		
Revenue Recognition Topic	**Existing Standard: FASB 5…**	**New Standard: ASC 606**
When Revenue is Recognized	• When realized or realizable *And…* • When earned[1] ✓ "Realized" – When goods, services, other assets are exchanged for cash or claims to cash.[1] ✓ "Realizable" – When goods, services, other assets are exchanged for readily convertible assets.[1] ✓ "Earned" – On delivery of goods or services, or other activities that constitute ongoing or central activities.[1]	• When each of the five contract criteria are met Or… ✓ Consideration nonrefundable ✓ One or more of the three additional contract criteria are met ➢ *This is a significant change from FASB 5, where cash basis revenue recognition can apply (see "Realized" in prior column).*

⇨ Difference: aspect of cash basis vs. meeting contract criteria

Details of the Revenue Recognition Model

2 Separate Performance Obligations In the Contract

Step 2: What *explicitly* or *implicitly* has been promised to the customer? Each promise is accounted for separately.

3 concepts drive the application of step 2:

- Distinct – Are the contract promises or performance obligations (POs) to the customer distinct?
- Standalone – In conjunction with "distinctness," can the goods or services be sold on a standalone basis?
- Integrating – Even if the goods or services are "distinct," are they interdependent or integrated in a contract?

Details of Step 2 of the Rev Rec Model

Distinct – Distinct goods or services are referred to as *performance obligations,* or a unit of account. A promise to transfer either of the following:

- "A good or service (or a bundle of goods or services) that is distinct."
- "A series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer."

! Each distinct PO is accounted for separately, and becomes it's own line item for contract administration.

Details of Step 2 of the Rev Rec Model

Distinct – "Distinct" has a very distinct meaning for ASC 606 purposes; a good or service must meet *both* of the following criteria to be distinct:

- Capable of Being Distinct – The customer can benefit from the good or service either on its own or together with other resources that are readily available.
- Distinct Within the Context of the Contract – The promise to transfer the good or service is separately identifiable from other promises in the contract.

⇨ Distinct also means the goods or services ***do not*** significantly affect each other.

Details of Step 2 of the Rev Rec Model

Standalone – "Distinct" can also be determined if the customer can benefit from the good or service on a "standalone" basis, or if they're regularly sold separately.

- The concept only goes so far; that is, even if a customer can realize "standalone value," they may not practicably be able to do so in the context of some contracts.
- This is where the application of "integrating" comes in.

! When PO's cannot be separated they need to be combined into a single line item for contract administration.

Details of Step 2 of the Rev Rec Model

Integrating – When goods or services are not distinct they're understood to be integrated; these instances can be identified as follows:

- The entity provides a significant service of integrating components of an offering (EG construction contract).
- The goods or services are highly interdependent upon each other, or highly integrated with each other.

! Non-distinct items should be combined into a single line item (bundled), with distinct items accounted for as separate line items for contract administration purposes.

Details of Step 2 of the Rev Rec Model

Independent vs. Interdependent – An entity assesses its POs for interdependence; related items are combined or bundled (a multi-element arrangement), with price allocation and/or reallocation to that bundle based on fair value (see step 4).

Scenario A: All POs Distinct	Independent Items
	PO1: Software License Software functional without updates or tech. support.
	PO2: Installation Service Routine; does not significantly affect customer's use.
	PO3: Software Updates Customers can benefit from updates together w/license.
	PO4: Technical Support Software can be used without technical support.

Scenario B: Two POs Combined	Interdependent Items
	PO1: Software License with Customized Installation A related set of POs bundled and interdependent in nature (high degree of customization required).
	PO2: Software Updates Customers can benefit from updates together w/license.
	PO3: Technical Support Software can be used without technical support.

A multi-element arrangement

Details of Step 2 of the Rev Rec Model

Existing Vs. New Standards: How Main Provisions Differ		
Revenue Recognition Topic	**Existing Standard: ASC 605-25**	**New Standard: ASC 606**
What is a Distinct Good or Service	• Can the customer benefit from the good or service or concept of "standalone value" ✓ Distinct goods or services accounted for as separate deliverables.[1] ✓ A *bundle* of goods or services is considered a deliverable, but there's greater ability to account for *separate* goods or services as deliverables –rather than recognition for the fulfillment of performance obligation with inter-related items (see ASC 606).	• A separate deliverable or performance obligation, *AKA* "unbundled" good or service ✓ Distinct goods or services accounted for as separate deliverables.[1] ✓ "Distinct" does not mean that revenue can be accounted for if the delivery of a *bundle* of goods or services is required to fulfil the performance obligation. In this case, the business would need to account for the bundle as a single performance obligation.

Details of Step 2 of the Rev Rec Model

Carve Outs for Step 2

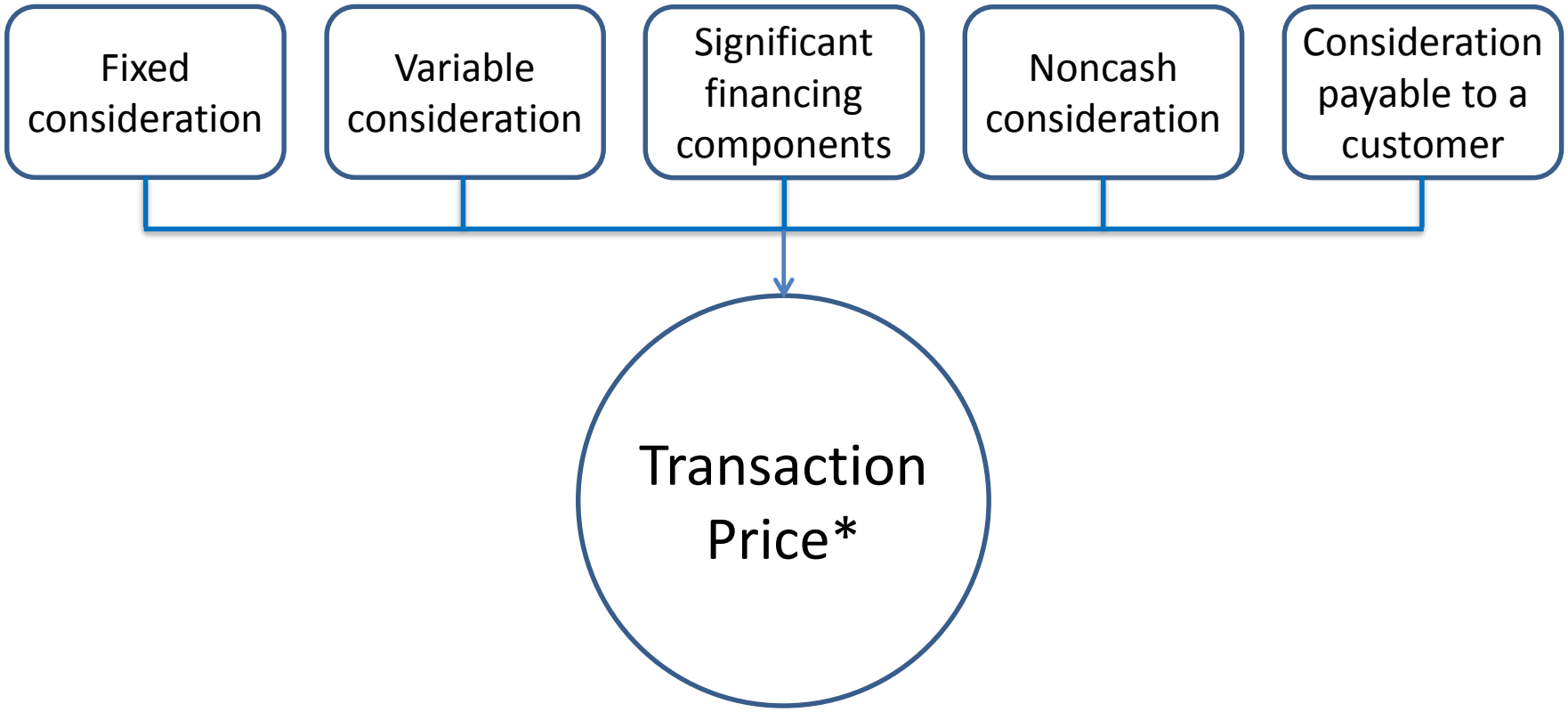
3 exceptions to the general principals:

- Service-Type Warranties – In connection with the sale of a product (whether a good or service).
- Options for Additional Goods or Services – Options to acquire additional goods or services for free, or at a discount.
- Nonrefundable Upfront Fees – A nonrefundable upfront fee at or near contract inception.

Details of the Revenue Recognition Model

3 Determine the Transaction Price

Step 3: Determine components of the transaction price



*Excludes sales taxes

Details of Step 3 of the Rev Rec Model

Accounting Contract Concept – For step 3, transaction amounts (price) reflects what the entity *expects to be entitled*, based on the customer's *potential to pay*.

∴ Step 3 uses an *allocated transaction price approach:*

<u>Uncertainties Measured</u>

- Variable consideration (single framework)
- Past practices with the customer

<u>Uncertainties Not Measured</u>

- Credit risk (no allowance recorded)

❗ Therefore, ASC 606 requires revenue ***booked at gross***

Details of Step 3 of the Rev Rec Model

Existing Vs. New Standards: How Main Provisions Differ		
Revenue Recognition Topic	**Existing Standard: ASC 605…**	**New Standard: ASC 606**
How Much Revenue is Recognized	**Legal Contract Concept –** Transaction amounts which the entity *contracts* to be entitled, based on *promises* to pay. **ASC 605-45 Accepted Approach** <u>Uncertainties Measured</u> • Credit risk (allowance recorded) <u>Uncertainties Not Measured</u> • Variable consideration (no single framework) • Past practices with the customer ⇨ Practices *measure rev. at net*	**Accounting Contract Concept –** Transaction amounts which the entity *expects* to be entitled, based on *potential* to pay. **Allocated Transaction Price App.** <u>Uncertainties Measured</u> • Variable consideration (single framework) • Past practices with the customer <u>Uncertainties Not Measured</u> • Credit risk (no allowance recorded) ⇨ Practices *measure rev. at gross*
	Despite the differences between existing and new standards, especially including the application of credit risk, many entities already follow the practices of gross revenue presentation, making practices comparable.	

Details of Step 3 of the Rev Rec Model

Separating Fixed from Variable Consideration		
Framework	**Fixed Consideration**	**Variable Consideration**
Definition	Future cash flows are known and predictable, with no enhancements or reductions from expected collections.	Future cash flows are uncertain; circumstances may either enhance, or reduce, from expected collections.
Simple Example	Contract calls for fixed price and quantity of amounts to be delivered.	Contract calls for variability in price and/or the quantity delivered.
Complex Example(s)	N/A	Contract calls for variability in considera-tion paid based on arrangements such as: • Product returns • Rebates • Discounts • Performance bonuses or penalties • Incentives
Revenue Recognition	Recognize revenue as performance obligations are met per contract requirements for delivery at said date(s).	Given lack of "constraints," recognize revenue as performance obligations are satisfied, including *estimates of the amounts the entity expects to be entitled at said date(s).*

Details of Step 3 of the Rev Rec Model

Drilldown on Variable Consideration: Prevailing Contract Conditions		
Framework	**Explicit Contract Conditions**	**Implied Contract Conditions**
Condition	Contract *explicitly says* the entity can realize more or less than the stated amount based on performance, or lack thereof.	Contract *implies* that the entity can realize more or less than the stated amount based on performance or lack thereof, if *either* of the following circumstances exist: • The customer has a *valid expectation* the entity will accept a different amount (less or more). • Facts and circumstances *indicate* a price concession will be offered, or an upcharge will apply.
"Less" Example	Performance penalty based on missing specific contract milestone/conditions.	Discounts, rebates, credits, and price concessions.
"More" Example	Performance bonus based on meeting specific contract milestone/conditions.	Enhancements, upcharges, or "tipping," which are a customary business practice.

Details of Step 3 of the Rev Rec Model

Estimates of Variable Consideration – Use either of the following methods, depending on which better predicts the amount of consideration the entity will be entitled:

- Expected Value – The sum of the probability-weighted amounts in a range of possible consideration amounts.
  - Appropriate if the entity has a large number of contracts with similar characteristics.
- Most Likely Amount – The single most likely amount in a range of possible consideration amounts.
  - Appropriate if the contract has two possible outcomes. Example: entity achieves a performance bonus, or not.

Details of Step 3 of the Rev Rec Model

Constraining Estimates of Variable Consideration – The "constraining event" prevents entities from including in estimates of variable consideration, revenue that is subject to reversal (to the extent it is *probable** that a significant reversal in the estimate will occur).

- Assessment of the "constraining event" is bound by both the *likelihood* and *magnitude* of the rev reversal.
  - Likelihood: Qualitative / Magnitude: Quantitative

❗ ASC 606 has an inherent downward bias; Viz. does not call for/incorporate upward or favorable adjustments.

*IFRS 15 specifies "*highly probable*"

Details of Step 3 of the Rev Rec Model

Reassessment of Variable Consideration – At the end of each reporting period, the entity must reassess revenue to be recognized from arrangements for variable consideration. Two factors must be taken into account:

- An assessment of "constraining event(s)," including the likelihood and magnitude of reversals.
- An update to reflect changes in price, quantity, or other factors affecting revenue recognition.

! FASB/IFRS: "…an entity should update its estimate[s]… [to] provide more useful information to users of [FS]."[1]

Details of Step 3 of the Rev Rec Model

Significant Financing Components – Two components may exist in a contract: Delivery of goods or services, and a *financing component; "significant financing"* is based on:

- The difference between the cash selling price and the agreed upon selling price for the goods or services.
- The length of time between the transfer of goods or services and the date the customer pays for them, *and* the prevailing interest rate at that time.

! If a "significant finance component" exists, the selling entity must assess either interest expense or revenue reflective of the time value of money, and recognize.

Details of Step 3 of the Rev Rec Model

Noncash Consideration – In exchange for goods or services an entity may also accept other noncash consideration from its customers.

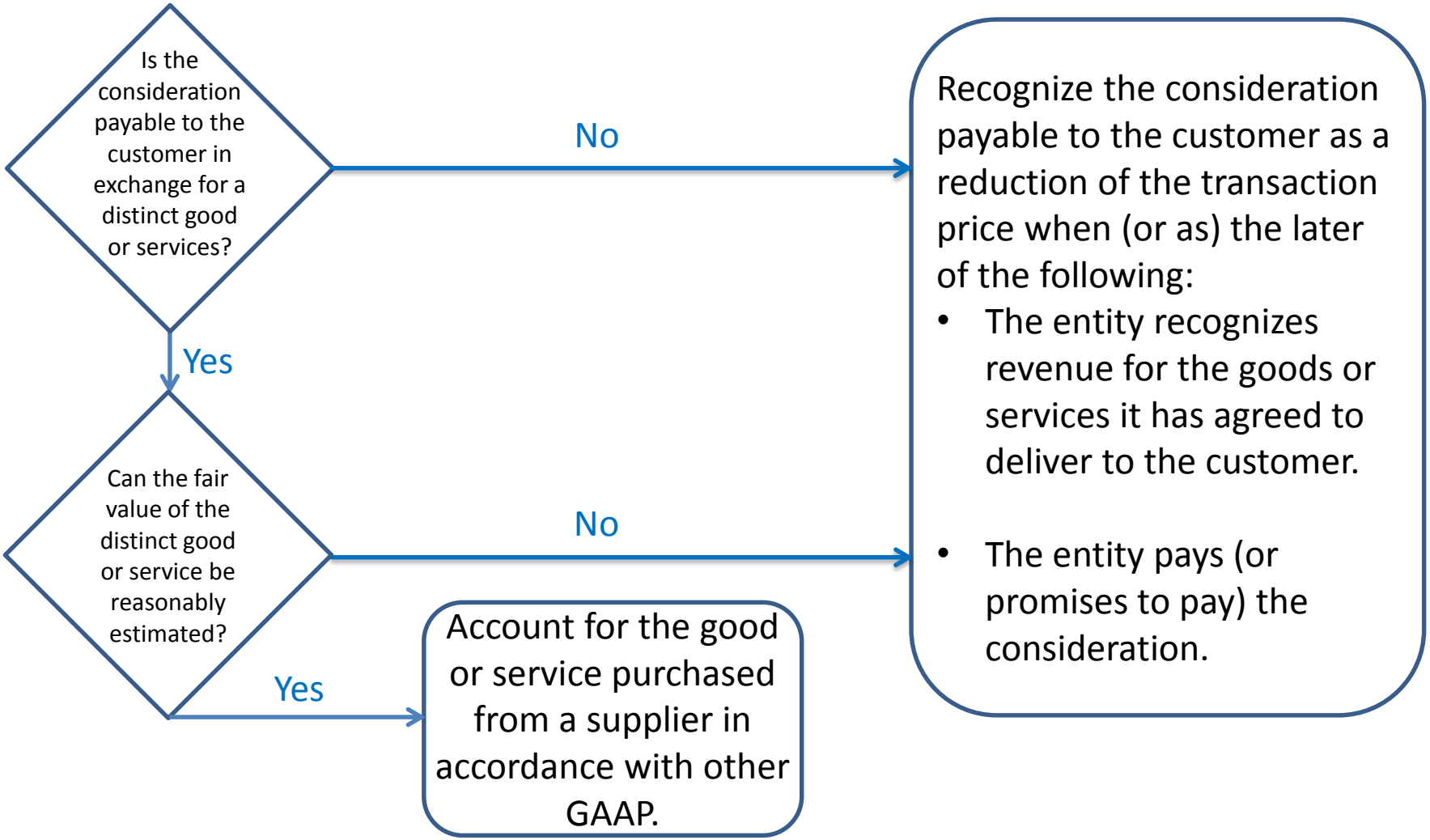
- Examples typical of such an exchange involve other goods, services, and/or stock.

! If "noncash consideration" exists, step 3 requires the recognition of the consideration at fair value at the contract date.

! If a customer contributes goods or services (materials, equipment, or labor) for the fulfillment of the contract, assess whether it obtains control, then recognize.

Details of Step 3 of the Rev Rec Model

Consideration Payable to a Customer – How to recognize[1]:



Details of Step 3 of the Rev Rec Model

Carve Outs for Step 3

Exception to the general principals for *sales or usage-based royalties related to licenses of IP.* For this use case, revenue may not be recognized until the later of:

- The subsequent sale or usage of the licensure occurs.
- The related sales-based or usage-based PO for has been satisfied (or partially satisfied).

! ASC 606 treats sales or usage-based royalties and those related to licenses of IP independently. Timing differences may exist for revenue recognition purposes.

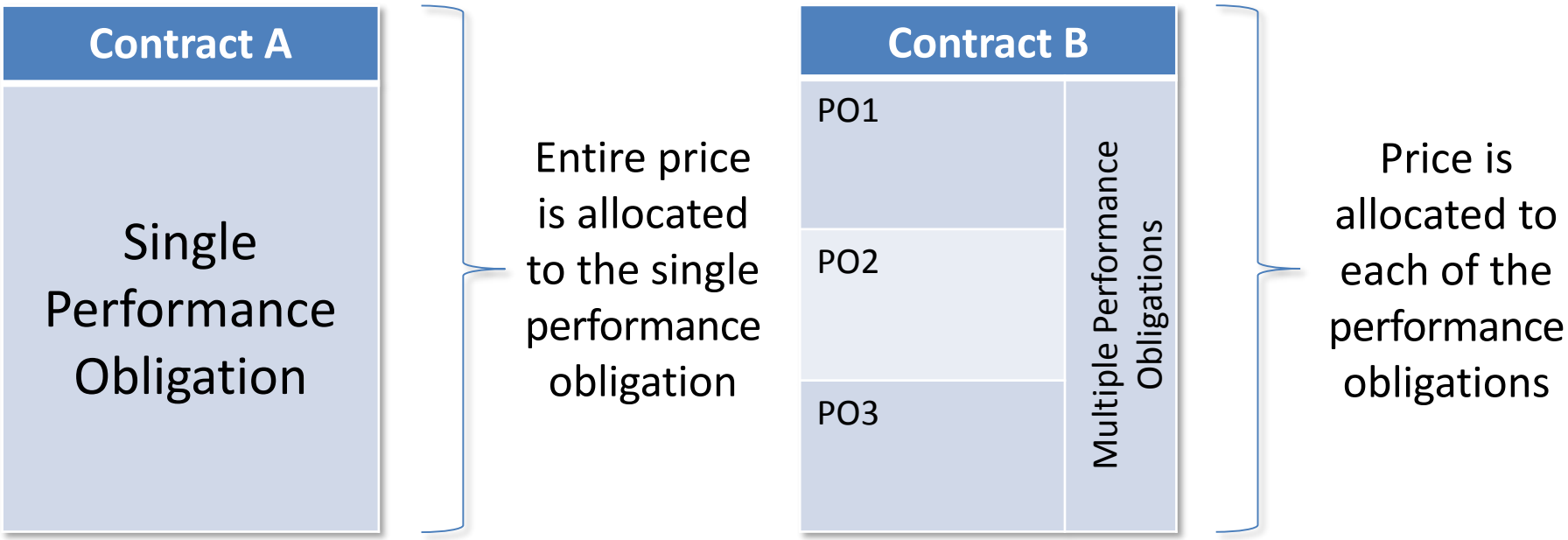
Details of Step 3 of the Rev Rec Model

Existing Vs. New Standards: Accounting for Recognition of Variable Consideration		
Framework	**Existing Standard: ASC 605**	**New Standard: ASC 606**
Singularity of Model	No single framework, with industry and transaction specific guidance (if any).	Single framework
Guiding Principal	Generally, guidance for revenue recognition required transaction selling price to be *"fixed or determinable."*	Guidance for revenue recognition is specific to the amount to which the entity *"expects to be entitled."*
Assessment on Guidance	"…the amount of revenue recognized is generally limited to the amount that is not contingent on a future event…"[1]	"…include an estimate of variable consid-eration (or contingent)…when the entity concludes will not result in reversals."[1]
Impacts of Variability	Dependent upon industry and/or transaction specific guidance	Two impacts of variability on rev rec: • Stated or implied conditions for dis-counts, rebates, returns, performance bonuses or penalties, incentives. • Contingency on the occurrence or nonoccurrence of a future event.
	⇨ "This less restrictive guidance will most likely result in earlier recognition of revenue under the ASU [606] than under current US GAAP"[1]	

Details of the Revenue Recognition Model

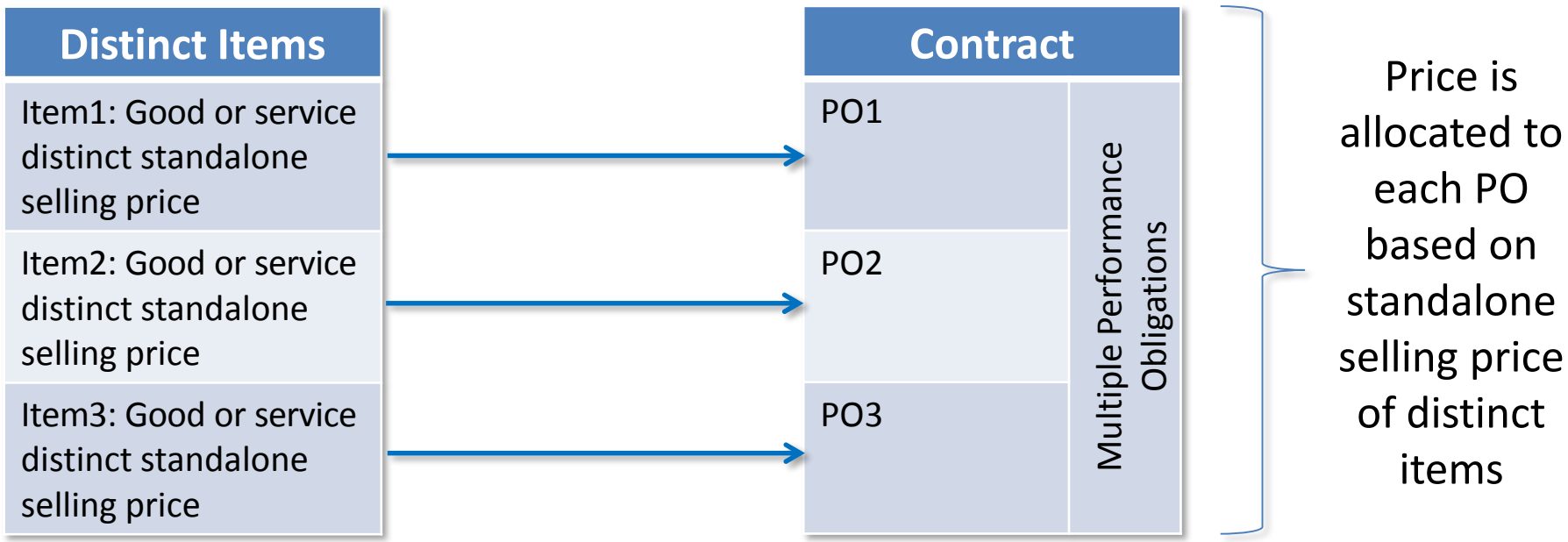
4 Allocate the Transaction Price to the PO's

Step 4: Requires allocating the transaction price determined in step 3 to the PO's identified in step 2.



Details of Step 4 of the Rev Rec Model

Allocation of Price – To determine the appropriate allocation of price to each PO, the ***standalone selling price*** of each distinct good or service at contract inception must be applied to those in the contract.



Details of Step 4 of the Rev Rec Model

Standalone Price Not Observable – If the *standalone selling price* of each distinct good or service at contract inception ***is not observable*** an entity ***must estimate it***.

Distinct Items
~~Item1: Good or service standalone selling price not observable~~
~~Item2: Good or service standalone selling price not observable~~
~~Item3: Good or service standalone selling price not observable~~

Prices for distinct items not observable so they must be estimated

Contract	
PO1	Multiple Performance Obligations
PO2	
PO3	

Prices for distinct POs must be estimated using one of three methods

Details of Step 4 of the Rev Rec Model

Estimation of Standalone Price – Given no observable price for distinct items in a contract, ***prices must be estimated*** using one of three methods:

- Adjusted Market Assessment Approach – Market price for goods or services (what market bears).
- Expected Cost Plus Margin Approach – Price for selling goods or services at cost, plus an appropriate margin.
- Residual Approach – Remaining price for goods or services in a bundle, when other items are observable.

⇨ Combining methods is acceptable if prices are variable

Details of Step 4 of the Rev Rec Model

Allocation of a Discount – A customer receives a contract discount for purchasing a ***bundle*** of goods or services if:

Standalone selling prices in bundle > consideration received

Two methods for allocating the discount:

Proportional	
PO1	Discount on All Items
PO2	
PO3	

No observable evidence of discount to one or more of the items in the bundle

Disproportional
PO1 Not Discounted
PO2 Separately discounted
PO3 Separately discounted

Observable evidence of discount to one or more of the items in the bundle

Details of Step 4 of the Rev Rec Model

Observable Evidence that Discounts Apply to One or More of the Items in the Bundle – For this use case, discounts *should be applied disproportionally,* if *all* of the following conditions are met:

- Entity regularly sells each distinct good or service (or each bundle of distinct goods or services) on standalone basis.
- Entity also regularly sells on a standalone basis a bundle (or bundles) at a discount to the standalone selling prices.
- Entity's discount on separate bundles (above bullet) equals the discount on the bundle sold.

Details of Step 4 of the Rev Rec Model

Allocation of Variable Consideration – An entity may be compensated for a *specified outcome(s).* This *variable consideration* may be attributable to the outcome of an entire contract, or a portion (distinct items) of the contract.

Entire Contract
Variable Consideration Applied

Variable consideration applied to contract as a whole

Distinct Items
Item1: Variable consideration for good or service
Item2: No variable consideration for good or service
Item3: No variable consideration for good or service

Variable consideration applied to a specific item(s)

Details of Step 4 of the Rev Rec Model

Variable Consideration – An entity allocates variable amounts –and subsequent changes to those amounts—to a portion (distinct or specific items) of the contract, if *both* of the following:

- Relates specifically to the *efforts of satisfying* the performance obligation, *or to a specific outcome*, related to transferring the distinct goods or services.
- Relates to the *amount of consideration* which the entity expects to be entitled in exchange for transferring the promised goods or services.

Details of Step 4 of the Rev Rec Model

Variable Consideration Applied to a Specific Item(s) – An entity allocates variable amounts –and subsequent changes to those amounts—to a portion (distinct or specific items) of the contract, if *either* of the following:

- One or more, but not all of POs in the contract, call for an entity to be compensated for *a* contingent outcome (EG a bonus for a single and specific outcome).
- One or more, but not all of POs in the contract, call for an entity to be compensated for *a series of* contingent outcomes (EG bonuses for a series of specific outcomes).

Details of Step 4 of the Rev Rec Model

Allocation of a Change in Price (Subsequent △Transaction Price) – After contract inception, changes in price may occur, in such instances as a change(s) in variable consid-eration. Allocation applies to all POs, or distinct items.

Proportional	
Item1	Change in price on all items (each item of type VC)
Item2	
Item3	

Change in price allocated to each item in the contract as all items were negotiated as variable consideration

Disproportional
Item1: Variable consideration for good or service
Item2: No variable consideration for good or service
Item3: No variable consideration for good or service

Change in price allocated to specific items in the contract as those items were negotiated as variable consideration

Details of Step 4 of the Rev Rec Model

Determining if a Change in Transaction Price Should be Applied to the Original Contract – Any changes in the transaction price should be allocated on the same basis as was negotiated at contract inception, *if*:

Criteria Met Vs. Criteria Not Met	
Criteria Met	**Criteria Not Met**
Prices for the delivery of goods or services change *due to* changes in variable consideration (viz. VC criteria met).	Prices for the delivery of goods or services change *but not due* to changes in variable consideration (viz. VC criteria not met).
Then, apply the change in price for goods or services *to those items only*.	Then, apply the change in price for goods or services *to all items*.
How: On the basis of the original negotiation for variable consideration of specific contract items.	How: On the basis of the initial relative stand-alone selling prices.

Details of Step 4 of the Rev Rec Model

Changes in Transaction Price – Other rules for subsequent change transaction price:

- The estimate of variable consideration is updated at each reporting period end date.
- Changes in transaction price(s) as contemplated here, exclude contract modifications.
- An entity should not reallocate the transaction price to reflect changes in the standalone selling price.

Details of the Revenue Recognition Model

5 Recognize Revenue as the Entity Satisfies PO's

Step 5: Requires recognizing revenue when (or as) the entity satisfies a PO by transferring a good or service.

Entity		Customer
PO1: Good or service is transferred to customer	→	PO1: Good or service is controlled by customer
PO2: Good or service is transferred to customer	→	PO2: Good or service is controlled by customer
PO3: Good or service is transferred to customer	→	PO3: Good or service is controlled by customer

Transfer is complete -and revenue recognized— when (or as) the customer obtains control

Details of Step 5 of the Rev Rec Model

Terms Related to Step 5:

- Asset – Goods or services transferred to and *used by* the customer.
- Control – Ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset.
- Period of Time – Sequential future periods where performance is satisfied and control of asset passes from entity to customer.
- Point-in-Time – Single point where control of asset passes from entity to customer (transfer at a distinct point).
- Input Methods – Method of rec rev over a *period of time* by measuring inputs toward satisfying a PO (EG labor hours expended).
- Output Methods – Method of rec rev over a *period of time* by measuring value delivered to the customer (EG milestones achieved).

Details of Step 5 of the Rev Rec Model

Existing Vs. New Standards: How Main Provisions Differ		
Revenue Recognition Topic	**Existing Standard: FASB 5…**	**New Standard: ASC 606**
When Revenue is Recognized	• When realized or realizable *And…* • When earned[1] ✓ "Realized" – When goods, services, other assets are exchanged for cash or claims to cash.[1] ✓ "Realizable" – When goods, services, other assets are exchanged for readily convertible assets.[1] ✓ "Earned" – On delivery of goods or services, or other activities that constitute ongoing or central activities.[1]	• When each performance obligation (or distinct goods or services) is satisfied.[2] ✓ Does not necessarily exclude delivery.[3] ✓ To depict the transfer of goods or services to customers, or when the entity *performs*.[4,5] ➢ *That is, when the entity performs it should recognize revenue (performance aligns with control; when the entity performs, the customer controls).*

⇨ Difference: receipt of assets, delivery vs. performance, control

Details of Step 5 of the Rev Rec Model

Period of Time Vs. Point-in-Time

Q: Can entities assume that they can recognize revenue over time rather than a point-in-time? A: No. ASC 606-10-25-27 to 29 requires ***one of the following criteria*** to be met for ***revenue to be recognized over time (viz. control of the asset is transferred over time, if):***

- The customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs.
- The entity's performance creates or enhances an asset. . . (EG work in process) that the customer controls as the asset is created or enhanced.
- The entity's performance *does not* create an asset with an alternative use to the entity . . . , ***and*** the entity has an enforceable right to payment for performance completed to date.

Details of Step 5 of the Rev Rec Model

Period of Time Vs. Point-in-Time, and Other Step 5 Issues

Q: What is the alternative? A: If a contract does not meet any of the criteria in ASC 606-10-25-27, the entity should recognize revenue at a ***point-in-time*** (ASC 606-10-25-30), rather than over time.

Q: When should the assessment should be made? A: At contract inception.

Q: Should the assessment as to whether to recognize revenue over time or at a point-in-time be made at the contract or performance obligation level? A: At the performance obligation level.

Q: Under ASC 606 is revenue recognized for goods at a point-in-time, while services over a period of time? A: It depends; the standard does not define performance and control for goods vs. services.

Details of Step 5 of the Rev Rec Model

While existing rev. rec. standards do not provide separate guidance for goods vs. services, they do have industry-specific guidance that generally aligns with either goods or services; ASC 606 *does not*, ***but the point remains***:

ASC 606 Control-Based Model	
Goods	**Services**
Generally, with the transfer of a good, control passes at a *point-in-time* (immediately).	Generally, with the transfer of a service, control passes *overtime* (future period(s)).

⇨ To restate, the fact pattern of performance and control for goods and services generally follows point-in-time, and period of time, respectively. However, some contracts, EG construction contracts, exhibit characteristics of both.

Details of Step 5 of the Rev Rec Model

Recognizing Revenue Over Time – If one of the three criteria for rec rev over time are met, then the entity must determine how far complete its progress is at any given reporting period (AKA *entity's measure of progress*).

- Methods of measuring progress, thus rev rec, include:
  - Output methods – Value of the goods or services delivered to date, relative to the remaining goods or services promised under the contract.
  - Input methods – Value of the inputs required to execute the contract to date, relative to the remaining inputs required to complete the contract.

Details of Step 5 of the Rev Rec Model

Recognizing Revenue Over Time (continued)

Q: Is the output or input method favorable? A: No. The entity must choose *a* method that most fully satisfies the objective of measuring completion of a performance obligation over the period of time.

Q: How should an entity rec rev (measure progress toward completion) on a cleaning service contract where service is rendered daily over a calendar year? What are acceptable input or output methods?

A: Time elapsed: Based on days passed. Output method.

A: Costs incurred: Based on a percentage of total expected costs to be incurred. Input method.

A: Labor hours: Based on a percentage of total expected hours logged vs. expected hours for the calendar year. Input method.

Details of Step 5 of the Rev Rec Model

Recognizing Revenue Over Time (continued)

Q: Can an entity use multiple methods for measuring progress (viz. a combination of output and input methods)? A: No. The entity must choose *a* method that most fully satisfies the objective of measuring completion of a performance obligation over the period of time.

Q: Should an entity apply a similar method to like performance obligations over its customer base (viz. apply consistently to similar POs in similar circumstances)? A: Yes. It should be applied similarly.

Q: How should an entity measure its progress toward completion of a performance obligation? A: At the end of a reporting period, the entity should remeasure its progress toward the completion of a performance obligation satisfied over a period of time.

Details of Step 5 of the Rev Rec Model

Recognizing Revenue Over Time (continued)

- Output methods, other standards and considerations
  - Disadvantages to method – Can be difficult and costly to observe where a "ramp-up," or a learning curve is evident.
  - Practical expedient – An entity can rec rev in the amount they have contracted to receive for their fixed hourly fees.
- Input methods, other standards and considerations
  - Examples – Input methods rev rec based on resources consumed, labor hours expended, machine hours used.
  - Abnormal waste – An entity should exclude from an input method costs of unexpected amounts for waste.

Details of Step 5 of the Rev Rec Model

Recognizing Revenue at a Point-in-Time – If one of the three criteria for rec rev over time are ***not*** met, then the entity must rec rev for the contract when *control of the goods or services is transferred* to the customer.

- Indicators of transfer of control include, but not limited to:
  - Entity has a present right to payment for the asset
  - Customer has legal title to the asset
  - Entity has transferred physical possession of the asset
  - Customer has the significant risks, rewards of ownership
  - Customer has accepted the asset

⇨ *Evidences* of the trigger point for recognizing revenue

Details of Step 5 of the Rev Rec Model

Recognizing Revenue at a Point-in-Time (continued)

Q: Do all indicators need to be evident to prove the transfer of control? A: No. They are indicating factors, not an all inclusive list.

Q: Is delivery a sufficient event to evidence the passage of control, and the recognition of revenue? A: Yes. If, at the point of delivery the customer accepts and takes control, and incurs an obligation to pay for the goods (the seller's contract would need to enforce these terms).

Q: Can an entity rec rev under a consignment agreement? A: No. If the goods are subject to a(n) consignment agreement, an entity should not rec rev upon delivery of a product (control is not established).

Q: Can an entity rec rev from a bill-and-hold arrangement? A: No. As the customer is not obligated to pay there's no evidence of control.

Details of Step 5 of the Rev Rec Model

Recognizing Revenue at a Point-in-Time (continued)

Q: How do shipping terms dictate when to recognize revenue?

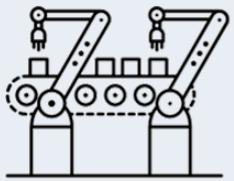
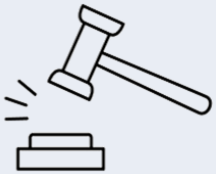
When to Recognize Revenue?

FOB Shipping Point — FOB Destination

How Shipping Terms Dictate Rev Rec per Free on Board (FOB) Shipping & Destination			
Consideration	**FOB Ship Point: Case I**	**FOB Ship Point: Case II**	**FOB Destination**
When Does Title Transfer?	To the customer at the entity's shipping dock	To the customer at the entity's shipping dock	To the customer at the customer's location
Scenario for Goods in Transit	Buyer is responsible for loss or damage	Seller assumes respons-ibility for loss or damage	Seller is responsible for loss or damage
When to Recognize Revenue?	Per five indicators for control, *when* customer controls, or at shipping point.	Per five indicators for control, *if* customer controls, then at shipping point.	Per five indicators for control, *when* customer controls, or at destina-tion point.

Details of Step 5 of the Rev Rec Model

Period of Time Vs. Point-in-Time: Examples of performance obligations and when control dictates revenue recognition.

ASC 606: Typical Revenue Recognition Patterns?			
Contract Manufacturing	**Construction Contract**	**Service-Type Warranty**	**Auction Sites**
			
Goods produced specific to contract requirements	Services to complete a contract for building	Service-type warranty associated with a product	Service to provide web-based price comparison
Revenue should be recognized at point of production (not at point of shipment), as goods have no alternative use according to 3-step criteria.	Revenue should be recognized at point-in-time (when completed), unless the entity proves evidence that one of the 3-step criteria are met.	Revenue from the service-type warranty component of a product sale should be separated and recognized over time (receives benefit over period of coverage).	Revenue (commission) should be recognized at point of click through, if the agent has an enforceable right to payment for click, not booking.

Subtopics of the Revenue Recognition Model

Subtopics of the Revenue Recognition Model

Contract Modifications

Scope: Contract modifications involving changes to price and/or scope, and their subsequent affect on the rec rev.

Source: ASC 606-10-25-12, 13 "Contract Modifications."
The Subtopic covers scenarios of modification, including:

- When changes are accounted for as a separate contract
- When changes are not accounted for as a separate contract, but a termination, modification, or both.

Examples: Agreement between parties to change contract

Approach: Determine if modification creates separate contract

Details of Contract Mod. of the Rev Rec Model

A modification to a contract is confirmed according to:

- Change in price or scope (or both) of the existing contract
- Both parties agree to change orally, in writing, or through another customary means in the business*

If there's a modification, then a determination must be made if its accounted for as a separate contract:

Contract Modifications: How to Account?	
Accounted for as a Separate Contract	**Not Accounted for as a Separate Contract**
• Wholly separate transaction	• Termination of the existing contract, and the creation of a new contract • Modification of the existing contract • A combination of the above two

*If parties have not agreed to change continue to account for contract using the existing agreement.

Details of Contract Mod. of the Rev Rec Model

Refresher on Terms Related to Contract Modification:

- **Distinct** – "Distinct" has a very distinct meaning for ASC 606 purposes; a good or service must meet *both* of the following criteria to be *distinct*:
  - **Capable of Being Distinct** – The customer can benefit from the good or service either on its own or together with other resources that are readily available.
  - **Distinct Within the Context of the Contract** – The promise to transfer the good or service is separately identifiable from other promises in the contract.

⇨ Distinct also means the goods or services ***do not*** significant affect each other.

- **Standalone Selling Price** – The price an entity would sell a promised good or service separately (indicates the customer can benefit from the product on its own).
- **Undelivered Goods or Services** – Goods or services from the original contract that have not been transferred at the date of contract modification.
- **Remaining Goods or Services** – The originally promised goods or services, *and* the newly promised goods or services from the contract modification.

Details of Contract Mod. of the Rev Rec Model

Accounted for as a Separate Contract: Wholly Separate Transaction – If the contract modification results in ***both***:

- Scope ***increases*** as defined by distinct goods or services added to the original contract.
- Price ***increases*** by an amount that reflects an entity's ***standalone price*** for the added goods or services sold.

…then the following according to ***ASC 606-10-25-12***:

- Original Contract: Fulfill – All undelivered POs from the original contract are treated as unmodified for the purposes of ASC 606.
- Separate Contract: Create – A new contract is created for those POs that conform to the increases in scope, and increases in price.

Details of Contract Mod. of the Rev Rec Model

Not Accounted for as a Separate Contract: Termination of the Existing Contract, and Creation of a New Contract – If the contract modification results in:

- Scope ***increases*** or ***decrease*** as defined by the delivery of remaining goods or services that are ***distinct***.
  OR
- Price ***increases*** or ***decrease*** for the remaining goods or services that are ***distinct***.

…then the following according to ***ASC 606-10-25-13(a)***:

- Original Contract: Terminate – Terminate the existing contract
- Separate Contract: Create – A new contract is created for those POs that conform to the increases or decreases in scope, or price.

Details of Contract Mod. of the Rev Rec Model

Not Accounted for as a Separate Contract: Modification of the Existing Contract – If the contract modification results in:

- Scope ***increases*** or ***decrease*** as defined by the delivery of remaining goods or services that are ***not distinct***.
  OR
- Price ***increases*** or ***decrease*** for the remaining goods or services that are ***not distinct***.

…then the following according to ***ASC 606-10-25-13(b)***:

- Original Contract: Modify – Additional goods or services are incorporated into the existing contract, with retroactive price treatment.

Details of Contract Mod. of the Rev Rec Model

Not Accounted for as a Separate Contract: Termination and Modification of the Existing Contract (Hybrid) – If the contract modification results in a combination of ***both***:

- Changes to contract PO(s) according to ***606-10-25-13(a)*** (changes to the scope or price of goods or services that are ***distinct***).
- Changes to contract PO(s) according to ***606-10-25-13(b)*** (changes to the scope or price of goods or services that are ***not distinct***).

…then the following according to ***ASC 606-10-25-13(c)***:

- Apply rules for each distinct PO (each part of the contract) according to either 13(a), or 13(b).
- No changes to rev rec for the fully satisfied POs is made.

Details of Contract Mod. of the Rev Rec Model

Not Accounted for as a Separate Contract: Modification of the Existing Contract – If the contract modification results in treatment according to *13(b), or 13(c) then*:

- Retroactive Price Treatment or Cumulative Catch-Up:

(Org. Consideration + Add. Consideration) * (Units Completed / Total Units) = A

(Org. Consideration * Org. % Complete (in $ terms)) = B

From Above: B – (minus) A = C / …then C + Total Remaining Consideration

- Example: Original contract for integrating widgets (not distinct)

Fact Pattern	Formula
• Original Contract: 10 widgets @ $10 each • Undelivered: 4 widget integrations • Modification: 15 more widgets @ $4 each	• ($100 + $60) * 20% = $32 ($100 * 40%) = $40 Cumulative catch-up = $8, w/$128 to rec.

Details of Contract Mod. of the Rev Rec Model

Not Accounted for as a Separate Contract: Comparison of treatments under 13(a), or 13(b):

Framework	Treatment under 13(a)	Treatment under 13(b)
Deliverable	Deliver 10 widgets	Integrate 10 widgets
Agreed Upon Price	$10 per widget	$100 for integration
Remaining Consideration	$50 (5 widgets delivered)	$60 (4 integrations complete)
Additional	Deliver 15 additional widgets	Integrate 15 additional widgets
Price for Additional	$4 per widget ($60 total)	$4 per widget ($60 total)
Additional Are Distinct?	Yes	No
Cumulative Catch-Up	No	Yes
Remaining Revenue to be Recognized	(5 * $10) + (15 * $4) = $110 Remaining Units = 20 $5.50 remaining rev rec (per unit)	($100 + $60) * 20% = $32 ($100 * 40%) = $40 ($8 catch-up) $128 remaining rev rec

Deloitte "A Roadmap to Applying the New Revenue Recognition Standard, 2017," p369

Subtopics of the Revenue Recognition Model

Licensing

Scope: Rev rec from contracts related to the licensing of intellectual property, or provides a customer right to IP.

Source: ASU No 2016-10 "Identifying Performance Obligations and Licensing." The update to Topic 606 covers:

- Sales- or usage-based royalties
- Right to use or right to access licenses

Examples: Software (some exceptions for hosting), movies, music, franchises, patents, trademarks, and copyrights.

Approach: Follows a specified version of the 5-step model

Details of Licensing of the Rev Rec Model

Terms Related to Licensing:

- License Transaction – Establishes a customer's right to, and control of, the IP (control is ability to direct, and benefit from, use of asset).
- Service Transaction – Does not grant the customer a right to, or control of, IP. EG Salesforce "license" which grants *service access*.
- Right to Use – A pattern of control which suggests the customer is granted the use of the IP at a point-in-time (AKA functional IP).
- Right to Access – A pattern of control which suggests the customer is granted the use of the IP for a period of time (AKA symbolic IP).
- Sales- or Usage-Based Royalty – An agreement which establishes a variable amount to be paid to the entity by the customer for the underlying sales or usage of the IP. EG a limited movie screening.

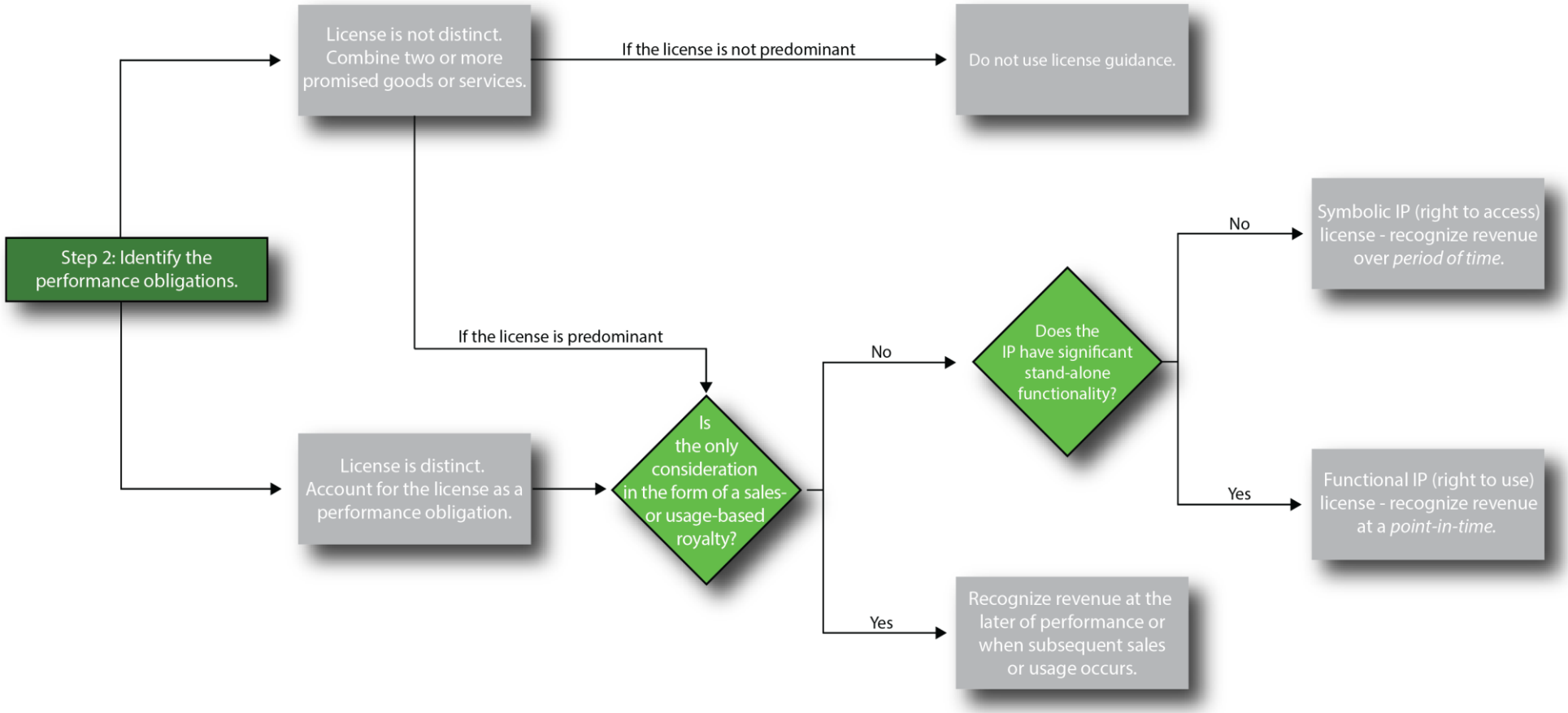
Details of Licensing of the Rev Rec Model

For revenue recognition from the use/licensing of IP to customers, apply a specified version of the 5-step model:

- Step 1: Identify the contract with the customer.
- Step 2: Separate POs in the contract. *Is the licensing of IP distinct within the context of the contract?*
- Step 3: Determine the transaction price which the entity expects to be entitled.
- Step 4: Allocate the transaction price to the individual POs.
- Step 5: Rec rev as the entity satisfies the POs, *with specificity regarding right to use vs. right to access IP.*

Details of Licensing of the Rev Rec Model

Licensing Principals Flowchart – PO Identification Forward



Deloitte "A Roadmap to Applying the New Revenue Recognition Standard, 2017," p433

Details of Licensing of the Rev Rec Model

Functional Vs. Symbolic Intellectual Property		
Framework	**Functional IP**	**Symbolic IP**
Right to	Use (makes underlying IP available for the customer's use and benefit)	Access (makes underlying IP available for customer's access and benefit)
Recognize Revenue	Point-in-time	Period of time
Standalone Functionality	Yes (utility derived from ongoing use of the IP for its operational activities)	No (utility derived from association with the entity's past or ongoing activities)
Examples	Software, biological compounds, drug formulas, films, television shows, music	Brands, team or trade names, logos, franchise rights

⇨ Notwithstanding differences in point-of-time vs. period of time benefit, an entity cannot rec rev until both are met:

- A copy of the IP is available for customer use
- Beginning of period customer is able to use and benefit

Details of Licensing of the Rev Rec Model

Carve Outs for Licensing Principals

2 exceptions to the general principals for licensing:

- Variable Consideration Related to Sales or Royalty Based Agreements – Does not follow other 606 guidance on VC; Rec rev only as POs are satisfied, *with no estimates* for what the entity expects to be entitled in the future.
- Hosted Software Arrangement – Excluded, unless it's portable; that is, unless the customer can both take possession, and run the software themselves. In this instance, customer controls, thus licenses, the software.

Subtopics of the Revenue Recognition Model

Costs Related to Contract

Scope: Capitalization and expensing of costs associated with customer contracts.

Source: Subtopic 340-40 "Other Assets and Deferred Costs – Contracts with Customers." The Subtopic covers:

- Incremental costs of obtaining a contract
- Costs incurred in fulfilling a contract not within the scope of another Topic

Examples: Commissions, T&E, due diligence, and direct costs

Approach: Separate direct and recoverable contract costs

Details of Costs of the Rev Rec Model

Existing Vs. New Standards: How Main Provisions Differ		
Cost Accounting	**Existing Standard[1]**	**New Standard: ASC 340-40**
Costs associated with obtaining and fulfilling a contract	• Allow companies to expense direct and incremental costs of obtaining a contract as incurred.	• Requires capitalization of incremental costs of *obtaining* and *fulfilling* a contract as incurred, if the entity expects to recover those costs. • If capitalized, as a deferred cost, to be amortized on a systematic basis consistent with the transfer of goods or services over the length of the contract, with anticipation of extension.
[1]While ASC 605-20 and ASC 310-20 provide guidance for the capitalization of certain precontract costs, including those related to warranties and loans respectively, other existing standards do not provide specificity on the treatment of contract costs (either pre or post-contract signing).		

⇨ Difference: Except where footnoted above, existing standards do not provide comprehensive guidance on contract costs.

Details of Costs of the Rev Rec Model

Capitalize Vs. Expense: Costs Related to Obtaining a Contract (Precontract Costs)		
Framework	**Capitalize**	**Expense**
Concept	An entity shall recognize as an asset the incremental costs of obtaining a contract, if the entity expects to recover those costs…costs that it would not have incurred if the contract had not been obtained…	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…
Method	Amortize in a manner that reflects the benefit (revenue) generated from the asset.	Expense as incurred
Exclusions	Any consideration payable to a customer (cash, credit, or coupons) for sales incentive.	Costs explicitly chargeable to the customer regardless of if the contract is obtained.
Examples	• 1st Yr. commissions for services	• 1st Yr. commissions for goods • T&E costs • Contract due diligence costs

Details of Costs of the Rev Rec Model

Treatment of Sales Costs in Obtaining a Contract:

- **Period of Time Vs. Point-in-Time** – Sales costs for a goods contract (delivered at a point-in-time) are expensed, while costs for obtaining a services contract (delivered over a periods of time) are capitalized.
- **Bundled Goods and Services Contracts** – Sales commission for obligations within a bundled goods and services contract follow rules as to delivered at a point-in-time vs. period of time. Viz. Expense commissions related to delivery, while capitalize those related to services.
- **Sales Costs Related to a Service Condition** – Sales commissions to be paid as contract service condition(s) are fulfilled/executed, should expensed as fulfillment occurs. These are not considered incremental costs.
- **Fringe Costs** – Fringe costs related to sales commissions for obtaining a contract should be treated similar to existing GAAP with respect to liabilities. Viz. if you record liability now, then capitalize for 606.
- **Spiffs for Sales Supervisors** – Supervisor's incentives for annual sales targets, overall profitability, etc., should be expensed as incurred, as they are not attributable (incremental) to identifiable contracts.

Carve Outs for Sales Costs (related to obtaining a contract)

Contracts of 1 Yr. or Less – As a practical expedient, costs related to a contract of one year or less can be expensed as incurred, but disclosure (footnotes) are required for such treatment.

Details of Costs of the Rev Rec Model

Capitalize Vs. Expense: Costs Related to Fulfilling a Contract		
Framework	**Capitalize**	**Expense**
Concept	Recognize as an asset the costs to fulfill a contract, if the costs meet all of the following criteria: • Directly related to a contract • Enhance resources for future PO's • Recoverable	Costs not directly related to a contract or an anticipated contract.
Method	Amortize in a manner that reflects the benefit (revenue) generated from the asset.	Expense as incurred
Exclusions	• Inventory • Preproduction costs for LT supply • Internal-use software • PP&E and computer hardware • Costs of software for sale, lease	N/A
Examples	• Direct labor • Direct materials • Direct costs allocable, chargeable	• G&A costs not related to PO's • Scrap, or other non-productive • Costs not attributable to PO's

Details of Costs of the Rev Rec Model

Treatment of Costs to Fulfilling a Contract

Capitalizing Fulfillment Costs – Costs related to the *future* fulfillment of a contract are capitalized "The costs generate or enhance resources of the entity that will be used in satisfying (or in continuing to satisfy) POs in the future." Viz. Initial costs that enhance future resources.

Expensing Fulfillment Costs – Costs related to the *ongoing* fulfillment of a contract are expensed "Costs that relate to satisfied POs (or partially satisfied POs) in the contract (that is, costs that relate to past performance)." Viz. Ongoing costs that do not enhance future resources.

Details of Costs of the Rev Rec Model

Cost Treatment for *Both* Obtaining & Fulfilling a Contract

- Amortization of Costs: Specific POs – Amortization of cost should be allocated to specific POs, not necessarily the contract as a whole "consistent with the goods or services to which the asset relates."
- Amortization of Costs: SL Method – If there is no distinguishable pattern of delivery with a contract (front-loaded, back-loaded, etc), amort. of the obtaining and fulfillment costs can be straight line.
- Amortization of Costs: Extensions – If the entity expects a contract extension, it should amort. deferred assets over that period as well.
- Impairment – An entity shall recognize an impairment in the P&L, *if*

  Deferred asset costs **>** Remaining consideration due – (minus) costs directly related to delivering the consideration

Sub-Topics of the Revenue Recognition Model

Presentation

Scope: Presentation of contract assets and liabilities, and their respective impact on the statement of activities.

Source: ASC 606-10-45-1 *cf.* "Other Presentation Matters." The Subtopic covers financial statement presentation of:

- Contract assets for conditional, unconditional rights
- Contract liabilities for conditional, unconditional rights

Examples: Line item presentation of activity in the statement of financial position, and statement of activities.

Approach: Determine classification of contract assets, liabilities

Details of Presentation of the Rev Rec Model

Terms Related to Asset Presentation

- Trade Receivable – 1) Unconditional right, with no contingencies, 2) subject to credit risk, not performance risk, 3) not recognized until collectibility is probable (prior to this, classified as Contract Asset), 4) reported gross –no netting of allowance(s) (presented separately as Allowance for Doubtful Account), Contract Assets, or rebates, 5) tested for impairment.
- Contract Asset – 1) Booked when at least a portion of the total contract PO(s) have been met (thus, some revenue recognized), 2) AKA unbilled receivable/revenue, 3) subject to performance risk *and* credit risk, 4) presented net of contract liabilities, 5) tested for impairment (allowance booked to Contract Liability), 6) per current and noncurrent classification.
- Deferred Costs – 1) Incremental costs of obtaining and fulfilling a contract as incurred, 2) amortized on a systematic basis consistent with the transfer of goods or services, 3) generally, noncurrent classification.

Details of Presentation of the Rev Rec Model

Terms Related to Liability and Net Presentation

- Contract Liability – 1) Consideration received in advance of performance, or unconditional right to consideration (which ever comes first), 2) AKA unearned/deferred revenue, 3) presented net of Contract Assets, 4) per current and noncurrent classification.
- Refund Liability – 1) Return provision in sales contracts for amounts paid or payable by the customer, 2) does not represent a liability for future performance, 3) stated separately from the contract assets and liabilities, 4) recorded as an estimate of the total returns anticipated (expectation of returns).

- Net Presentation of Contract Assets and Liabilities – An entity must present *net* its contract assets and liabilities *for the same contract* on the face of the balance sheet.

Details of Presentation of the Rev Rec Model

Concepts Related to Impairment

- The following are subject to impairment testing:
  - Receivables – Per FASB Topic 310
  - Contract Assets – Per FASB Topic 310
  - Deferred Costs – Per FASB Topic 340 (40-35-3)
  - ⇨ The objective of testing is to determine if the carrying amount of the related balances are recoverable, if not, then impaired.
- Specific to receivables and contract assets, the new rev standard is not intended to supplant existing GAAP (Topic 310) with respect to measurement, presentation, and disclosure. Thus, accounting.
- Step 1 redux: 606 only allows revenue recognition if all five measures of a contract are in place, including *probability of collection*.

Details of Presentation of the Rev Rec Model

Collectibility is Probable			Collectability is Not Probable		
All five steps of the contract model are met, including probability of collection.			All five steps of the contract model are *not met*, as to doubt of collection.		
Contract is valid for 606 purposes; rev rec to the full value of the contracts, with accompanying allowance managed according 310.			Contract is not valid for 606 purposes; rev rec ceases at an amount up to the revised estimate for collectibility, with balance deferred.		
For a portfolio, collectibility for each contract is probable, but a 2% valuation allowance is applied consistent with accounting per 310. For this scenario, POs have been satisfied.			For a specific contract, collectibility is estimated at 80%; rev is deferred, with the resulting contract rec. and asset tested for impairment. For this scenario, POs have been satisfied.		
Account	**Debit**	**Credit**	**Account**	**Debit**	**Credit**
Trade Receivables	$1,000		Trade Receivables	$800	
Contract Revenue		$1,000	Unbilled Revenue	$200	
Contract Impairment Loss	$20		Deferred Revenue		$200
Allow. for Doubt. Acc't		$20	Contract Revenue		$800

Details of Presentation of the Rev Rec Model

Thumbnail Presentation of Statement Balances

Presentation of Statement of Financial Position & Statement of Activities				
Statement of Financial Position			**Statement of Activities**	
Assets	**Gross or Net**		**Revenue**	**Gross or Net**
Trade Receivables	Gross		Contract Revenue	Gross
Allow. for Doubt. Acc't	Gross		Reimbursed Expenses	Gross*
Unbilled Revenue	Net			
Deferred Costs	Gross			
			SG&A Expenses	
Liabilities			Contract Costs	Gross
Deferred Revenue	Net		Contract Impairment Loss	Gross
Refund Liability	Gross			

*Not net against expense, if entity assumes payment risk or liability (carries cost).

Details of Presentation of the Rev Rec Model

Transition – An entity must elect a transition method from 605 to 606. This affects FS presentation as follows:

- Full Retrospective Approach – The BS and P&L *are restated* for all contract balances affected as of the beginning date two years prior to the date of adoption.
- Modified Retrospective Approach – The BS and P&L *are not restated*, but a cumulative catch-up adjustment is made as of the beginning date of the year of adoption.

❗ For mod. approach, elect to apply to all contracts at the begin date, OR only those not completed at the begin date.

Details of Presentation of the Rev Rec Model

Transition Approach (method) from ASC 605 to ASC 606

Transition Approach (Method) and Accompanying Dates of Effectiveness			
Transition Approach / Method	Date of Financial Restatement	Date to Apply 606 to Contracts Presented	Date of Cumulative Effect of Adjustment
Full Retrospective[1]	Two year prior to date of adoption re-state FS balances	Two years prior to date of adoption	Two years prior to date of adoption for all contracts
Modified Retrospective (AKA Cumulative Effect)[2]	Do not restate FS balances	Date of adoption	Date of adoption for either all contracts OR those in-progress

Notes:

[1]Assumes two years of comparative (prior year) financial statement information presented.

[1,2]Changes apply to all affected line items, both revenues and associated contract expenses.

[2]An entity can elect to apply the cumulative effect to either all prior contracts, OR only those prior contracts which are in-progress as of the beginning date of the year of adoption. For either, the cumulative adj applies to the prior two years of difference between 605 and 606.

Details of Presentation of the Rev Rec Model

Transition Approach (method) from ASC 605 to ASC 606

Transition Approach (Method) and Impact on Financial Statement Presentation			
Transition Approach / Method	Line Item Disclosure in Year of Adoption	Comparability of Results	Prior Restatement of Contracts
Full Retrospective	None	Yes, comparability of contract revenue and expenses are available for years of FS presentation.	Yes, contracts begin-ing two years prior to the date of adop-tion need to be restated.
Modified Retrospective (AKA Cumulative Effect)	Yes, entity will need to present compar-ative 605 vs. 606 schedules for all line items affected.	No, cumulative nature of adjust-ment prevents full comparability of FS balances presented.[1]	No, contracts completed prior to the adoption date do not need to be restated.

[1]Separate schedules for all lines items affected will provide a stop-gap for comparability, but on separate schedules, and not directly on face of P&L.

Details of Presentation of the Rev Rec Model

Full Retrospective Approach

Scenario: Entity adopts ASC 606 in January, 2018, and elects the full retrospective approach. The Co. must analyze the full extent of its need to restate, by comparing revenue recognized under ASC 605, to revenue it would have recognize under ASC 606. The following entries are booked, as required, to restate its balance sheet and profit and loss.

Step 1: Restate balance sheet for transition

Entries posted as of 01/01/16.

If revenue was *accelerated* into earlier periods:

Account	Debit	Credit
Contract Asset	$750	
Retained Earnings		$750

If revenue is *deferred* into later periods:

Account	Debit	Credit
Retained Earnings	$750	
Contract Liability		$750

Step 2: Restate profit and loss for transition

Entries posted as of 12/31/16, and years following.

If revenue was *accelerated* into earlier periods:

Account	Debit	Credit
Revenue	$250	
Contract Asset		$250

If revenue is *deferred* into later periods:

Account	Debit	Credit
Contract Liability	$250	
Revenue		$250

Details of Presentation of the Rev Rec Model

Modified Retrospective Approach

Scenario: Entity adopts ASC 606 in January, 2018, and elects the modified retrospective approach. The Co. must analyze the full extent of its need to cumulatively adjust, by comparing revenue recognized under ASC 605, to revenue it would have recognize under ASC 606. The following entries are booked, as required, to affect its balance sheet and P&L.

Step 1: Adjust balance sheet for transition
Entries posted as of 01/01/18.
If revenue was *accelerated* into earlier periods:

Account	Debit	Credit
Contract Asset	$500	
Retained Earnings		$500

If revenue is *deferred* into later periods:

Account	Debit	Credit
Retained Earnings	$500	
Contract Liability		$500

Step 2: Adjust profit and loss for transition
Entries posted as of 12/31/18, and year following.
If revenue was *accelerated* into earlier periods:

Account	Debit	Credit
Revenue	$250	
Contract Asset		$250

If revenue is *deferred* into later periods:

Account	Debit	Credit
Contract Liability	$250	
Revenue		$250

Sub-Topics of the Revenue Recognition Model

Disclosure

Scope: Disclosure requirements related to the nature, timing, and uncertainty of revenues and cash flows from contracts.

Source: ASC 606-10-50-1 *cf.* "Disclosures." The Subtopic covers disclosure requirements related to the following:

- Qualitative and quantitative info. regarding contracts
- Significant judgements, and assets related to contract costs

Examples: Schedules of contract assets, liabilities, and revenue, disaggregated, and supported by qualitative analysis.

Approach: A framework for the consistent analysis of rev rec

Details of Disclosure of the Rev Rec Model

Select Quantitative Disclosures and Practical Expedients

Select Disclosure Schedules and Practical Expedients		
Disclosure Schedule	**Schedule Requirement**	**Non-Public Practical Expedient**
Disaggregation of revenue from contracts	Reconciliation of contract rev rec according to product line, market vertical, geography, and timing.	Yes, but must present revenue by point-in-time (goods) vs. period of time (services).
Opening and closing balances of contract assets and liabilities	Presentation of contract assets and liabilities with opening, closing, and net changes over multi-year period.	None
Revenue recognized from past perfor-mance	Reconciliation of "out of period" adjustments due to a change in estimates of contract values.	Yes
Transaction price allocated to remaining POs	Presentation of contract backlog with schedule for fulfillment and recognition of remaining POs.	Yes. Also practical expedient for public entities with contracts less than one year.

Details of Disclosure of the Rev Rec Model

How do I architect my business systems
to provide for the disclosure requirements?

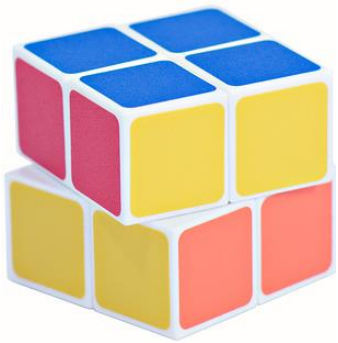
Entities will need to capture data
related to their contracts according to…

specified financial (GL)
account balances

Account No	Account Description
20000	A/R: Trade
50900	Deferred Rev - Billed
50900-01	Deferred Rev - Unbilled
99999-01	Unbilled AR

separate books
(605 vs. 606)*

segments like product line,
service type, geo., etc.



***Aids in transition to 606, and comparative requirements of 606 vs. 605**

Details of Disclosure of the Rev Rec Model

Drilldown on GL Account Balances – Capturing data to support disclosures for contract assets, liabilities, revenue, and cash flow requires the following GL account schema:

Contract GL Accounts, Definitions & Attributes		
Contract Metric	**Definition**	**Where**
Unbilled Accounts Receivable	Contracted Backlog Not Billed	Face of BS*
Unbilled Deferred Revenue	Contracted Backlog Not Earned	Face of BS*
Unbilled Sales Revenue	Amounts Earned Not Billed	Face of P&L*
Billed Accounts Receivable	Amounts Billed Not Paid	Face of BS
Billed Deferred Revenue	Amounts Billed Not Earned	Face of BS
Billed Sales Revenue	Revenue Earned Not Paid	Face of P&L
Paid Deferred Revenue	Amounts Billed and Paid, Not Earned	Face of BS
Paid Sales Revenue	Revenue Earned and Paid	Face of P&L
*All three are presented on face of financial statements or posted to non-GAAP GL accounts		

Details of Disclosure of the Rev Rec Model

Sample Presentation: Disaggregation of Revenue

Disaggregation of Revenue from Contracts						
Segment		**Consumer**	**Transport**	**Energy**		**Total**
North America	$	1,155	8,971	9,874	$	20,000
Europe		4,155	10,578	12,457		27,190
Major Goods or Services						
Appliances		2,411	13,438	7,697		23,546
Plant Feasibility Study		2,899	6,111	14,634		23,644
Timing of Rev Rec						
Goods Xfer'd at Point-in-Time		714	11,293	5,310		17,318
Services Xfer'd Over Time	$	4,596	8,256	17,021	$	29,872

Source: IFRS Taxonomy 2017, example 41

Details of Disclosure of the Rev Rec Model

Sample Presentation: Opening and Closing Balances

Opening and Closing Balances of Contract Assets and Liabilities						
Year of Posting		**Contract Receivables**	**Contract Assets**	**Contract Liabilities (ST)**		**Contract Liabilities (LT)**
2018						
Opening: 01/01/18	$	13,788	9,565	13,013	$	1,978
Closing: 12/31/18		14,138	9,978	13,477		2,176
2018 Inc / (Dec)		350	413	464		189
2017						
Opening: 01/01/17		12,465	9,178	12,788		1,778
Closing: 12/31/17		13,788	9,565	13,013		1,978
2017 Inc / (Dec)	$	1,323	387	225	$	209

Details of Disclosure of the Rev Rec Model

Sample Presentation: Rev Rec from Past Performance

Revenue Recognized from Past Performance					
Consideration		**Original Amount**	**Adjusted****		**Recognized**
Fixed	$	23,000	23,000	$	11,500
Variable*		4,800	4,800		2,400
Total Potential Consideration	$	27,800	27,800	$	13,900
Cumulative Adj. for Earning Variable Consideration (remaining variable)				$	2,400

*Contract calls for bonus/variable consideration for meeting performance qualifications.
**Adjust to total potential as entity looks to recognize all variable consideration for meeting agreed upon performance qualifications.

Type	Fixed Consideration	Variable Consideration
Definition	Future cash flows are known and predictable, with no enhancements or reductions from expected collections.	Future cash flows are uncertain; circumstances may either enhance, or reduce, from expected collections.

Details of Disclosure of the Rev Rec Model

Sample Presentation: Transaction Price Allocated to POs

Transaction Price Allocated to Remaining POs (AKA Backlog)						
Contract Type Grouping		**2018**	**2019**	**2020**		**Total**
Appliances	$	7,800	4,550	1,345	$	13,695
Plant Feasibility Study		8,950	6,475	3,575		19,000
Consumer Products		1,225	975	445		2,645
Manufactured Parts		2,775	2,600	1,350		6,725
Total Contract Groupings	$	20,750	14,600	6,715	$	42,065

Reported backlog is for contracts greater than one year that are unsatisfied or partially satisfied. Contract presentation per major good or service category.

Systems for 606: Managing Revenue in the New Economy

Systems for 606: Managing Revenue

What system considerations do CFOs have in managing revenue in the new economy?

Contract Management

Subscription-Based Billing

ASC 606/IFRS 15 Compliance

Systems for 606: Managing Revenue

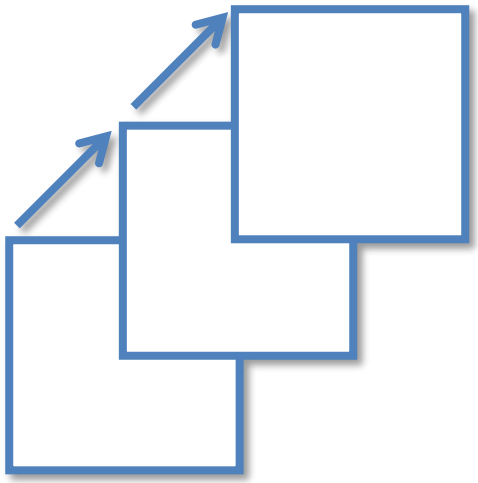
…and what capabilities must their systems have to manage revenue in the new economy?

- Contract segmentation (dimensioning)
- Non-linear billing schedules
- Complex pricing schedules with fair value
- Concurrent expense amortization
- Reporting for contracts, backlog, cash flow

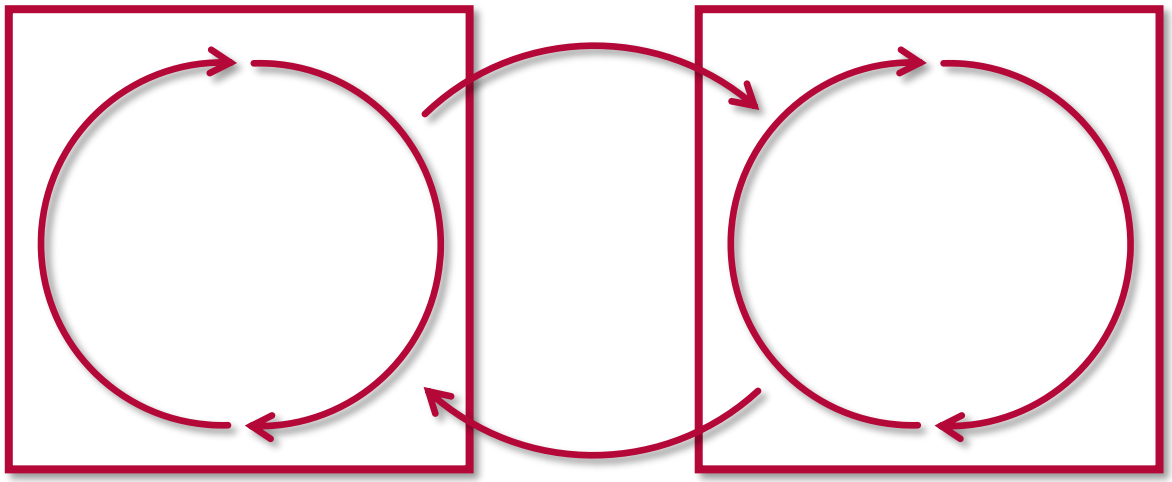
Systems for 606: Managing Revenue

System Architecture – To mirror actual contract activity, and meet 606 requirements, CFOs need *a* system whose architecture manages workflow within a single transaction.

Legacy System(s)	606 System	CRM System
Multiple Transactions*	Single Transaction	Single Transaction



*Or, multiple systems approach

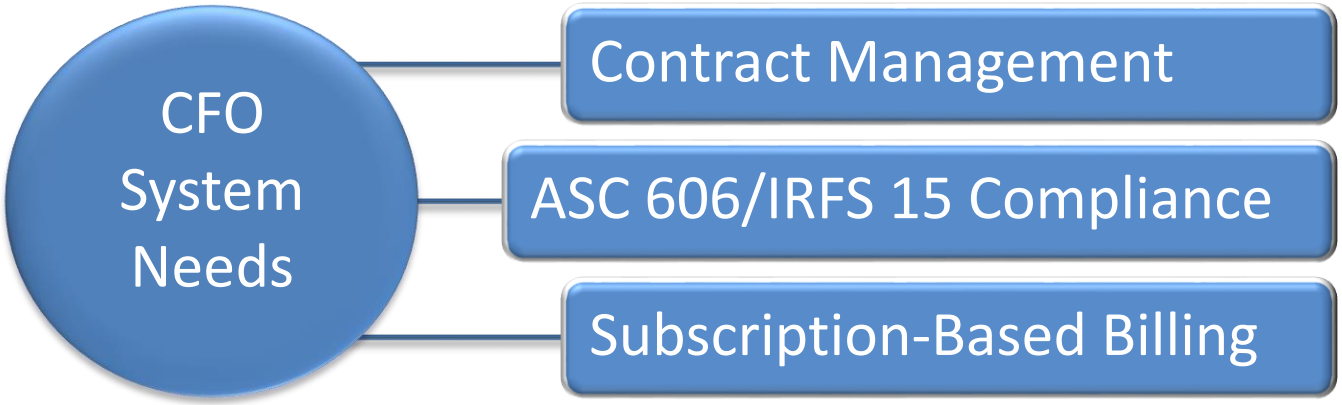


The Contract object is both dynamic for the parameters of the original contract, and dynamic for modifications to the contract.

Systems for 606: Managing Revenue

Functional System Requirements to Support CFO Needs

Managing Contracts with Customers in the New Economy		
Contract Management	**ASC 606/IRFS 15 Compliance**	**Subscription-Based Billing**
• Continuous workflow • Practical accounting • CRM integration • Non-linear pricing • Non-linear billing	• Contract identification* • Bundling or MEA** • Allocation/reallocation • Transition from ASC 605 • Concurrent exp. mgm.'t	• Usage metering • Recurring invoicing • Renewal management
*Using Contract dimension	**For interdependent items or multi-element arrangements	



Systems for 606: Managing Revenue

Main Provisions of 606 as Applied to Systems

1. Model: Identify the Contract
   System: Contract Object
2. Model: Separate Performance Obligations
   System: Contract Line Item
3. Model: Determine Transaction Price
   System: Line Item Fixed or Variable Amount
4. Model: Allocate Transaction Price
   System: MEA Price List, Allocation, Reallocation
5. Model: Recognize Revenue
   System: Revenue Templates and Schedules

Systems for 606: Managing Revenue

606 Impact on Co.'s Managing Standardized Agreements – Legacy systems will likely support businesses managing:

- Ship & Bill Contracts – Standardized goods shipment, where performance is coincident with benefit.
- Time & Materials Arrangements – Time of performance is coincident with benefit of service.
- Simple Subscription Agreements – Delivery of independent performance obligations.

! Caveat: For 606, auditability is per contract, not invoice or customer! Thus, contract report segmentation is absent.

Systems for 606: Managing Revenue

606 Impact on Co.'s Managing Variable Agreements – Legacy systems will not support businesses managing:

- Long-term contracts
- Interdependent performance obligations
- Variable pricing
- Agreements subject to modification

! Because 606 forces a match between performance and benefit, systems will need greater flexibility for managing price allocation, and the timing of recognition.

Systems for 606: Managing Revenue

System Architecture for Addressing Contracts with Customers		
System Element	**As Is (Legacy) Systems**	**To Be (606) Systems**
Contracts, performance obligations (POs)	Possible, but generally satisfied by repurposing other objects	Dedicated objects, including dimensions
Customer transactions (order or invoice)	Static or closed	Dynamic
Revenue journal and reporting book	Single	Multiple
Performance obligations	Lumped together as a single item; E.G. PCS (post-contract support)	Distinct line items, with specific delivery, allocations, rev rec
Multi-element arrangement (MEA) or bundles	If POs don't have FV, then bundle accounted for as a single transaction and deferred (VSOE)	Each PO must have FV, and recog-nized as delivered, according to relative selling price method
Backlog and CF reports related to deferred revenue, assets, liabilities	Likely offline (compliance for non-public Co.'s less likely)	Likely online (additional disclosures for non-public Co.'s)
Concurrent contract expense amort according to contract period	Manual or separate module for tracking, with no contract tie-in	Contract expense amortization integrated with contract mgm.'t

⇨ 606 makes multiple systems approach operationally difficult

Systems for 606: Managing Revenue

Checklist for New Systems – CFOs need to consider the following for systems, and a migration path to them:

- Roadmap detailing transition of systems and processes
- ERP architected for contract and 606 management
- CRM and ERP integration for joint contract management
- Revised data model to support contract reporting
- Conversion of legacy transactions into contract balances
- Coordination with auditors for 606 transition approach
- Legal review of contracts for determination of POs

Appendix

Appendix: Terminology

Terminology (as defined by FASB, unless otherwise noted):

- **Contract** – An agreement between two or more parties that creates enforceable rights and obligations.
- **Contract Asset** – An entity's right to consideration in exchange for goods or services that the entity has transferred to a customer when that right is conditioned on something other than the passage of time (for example, the entity's future performance).
- **Contract Liability** – An entity's obligation to transfer goods or services to a customer for which the entity has received consideration (or the amount is due) from the customer.
- **Customer** – A party that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration.
- **Performance Obligation** – A promise in a contract with a customer to transfer to the customer either: 1) a good or service (or a bundle of goods or services) that is distinct, 2) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.
- **Probable** – The future event or events are likely to occur.
- **Revenue** – Inflows or other enhancements of assets of an entity or settlements of its liabilities (or a combination of both) from delivering or producing goods, rendering services, or other activities that constitute the entity's ongoing major or central operations.

Appendix: Terminology

Terminology (as defined by FASB, unless otherwise noted):

- **Standalone** – Dependent upon whether the goods or services are sold on a standalone basis.[1]
- **Standalone Selling Price** – The price an entity would sell a promised good or service separately [indicates the customer can benefit from the product on its own].
- **Transaction Price** – 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 3rd parties.
- **Fixed Consideration** – Future cash flows are known and predictable, with no enhancements or reductions from expected collections.[1]

.

- **Variable Consideration** – Future cash flows are uncertain; circumstances may either enhance, or reduce, from expected collections.[1]
- **Remaining Performance Obligations** – Designate of "backlog," (EG amounts shown on a "backlog report), or remaining contractual value, not yet recognized as a contract asset.[1]
- **Right to Invoice** – Designate of variable pricing, used, for example, in a usage-based pricing arrangement.[1]

[1]Not a FASB definition

Appendix: Terminology

Terminology (as defined by FASB, unless otherwise noted):

- **Distinct** – A good or service must meet both of the following criteria to be distinct:

  1) Capable of Being Distinct – The customer can benefit from the good or service either on its own or together with other resources that are readily available.

  2) Distinct Within the Context of the Contract – The promise to transfer the good or service is separately identifiable from other promises in the contract.

  Distinct also means the goods or services do not significantly affect each other.[1]

- **Independent** – Good or services that are not highly dependent upon each other for the performance of the contract, or components of the contract. These performance obligations may be sold together, but would not constitute a "bundle" for the purposes of revenue allocation under ASC 606.[1]

- **Interdependent** – Goods or services that are highly integrated, or dependent upon each other for the performance of the contract, or components of the contract; often considered in the context of a bundle (Viz. a related set of POs bundled and interdependent in nature where there is a high degree of customization required).[1]

[1]Not a FASB definition

Appendix: Standards, Body of Standards

Standards, Body of Standards

- **FASB** – Financial Accounting Standards Board responsible for US GAAP.
- **IASB** – International Accounting Standards Board responsible for IFRS (International Financial Reporting Standards).
- **FASB/IASB** – The boards issuing final (joint) standards on changes to accounting for revenue per contracts.
- **ASC 605-35** – The codification (Accounting Standards Codification) of ASU 2010-17; rev rec: Construction-Type and Production-Type Contracts (provides guidance for these arrangements).
- **ASU 2014-09** – The joint standard (Accounting Standards Update) issued by FASB for accounting for revenue from contracts. Additional ASU's followed for clarifications (ASU 2015-14, 2016-08, 10, 12).
- **ASC 606** – The codification (Accounting Standards Codification) of ASU 2014-09; ASC the source of authoritative GAAP recognized by FASB.[1]
- **IFRS 15** – The joint standard (International Financial Reporting Standard) issued by IASB for accounting for revenue from contracts.

Appendix: Standards, Body of Standards

Standards, Body of Standards

- **FASB 5** – Existing US GAAP guidance on rev rec AKA, Statement of Financial Accounting Concept (SFAC) No. 5, Recognition and Measurement in Financial Statements of Business Enterprises.
- **FASB 6** – Existing US GAAP guidance on rev rec (definition of "revenue"). AKA, Statement of Financial Accounting Concept No. 6, Elements of Financial Statements.
- **ASC 605-10** – Existing US GAAP guidance on revenue recognition –Overall; Codification of FASB 5.

Preparing for Change

Tactics to help CFOs achieve optimal performance with the new revenue standards and economy.

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