ASC 606 Revenue Recognition

It's Here. Are You Ready?

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What Is ASC 606?

In May of 2014, the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) together issued a new accounting standard: ASC 606 “Revenue from Contracts with Customers Standard” or “the Standard”. The Standard simplifies how companies record revenue from customer contracts. Effective 2018 for public companies and 2019 for private companies, it covers how businesses report the nature, amount, and timing of customer contracts.

Overview of Significant Changes

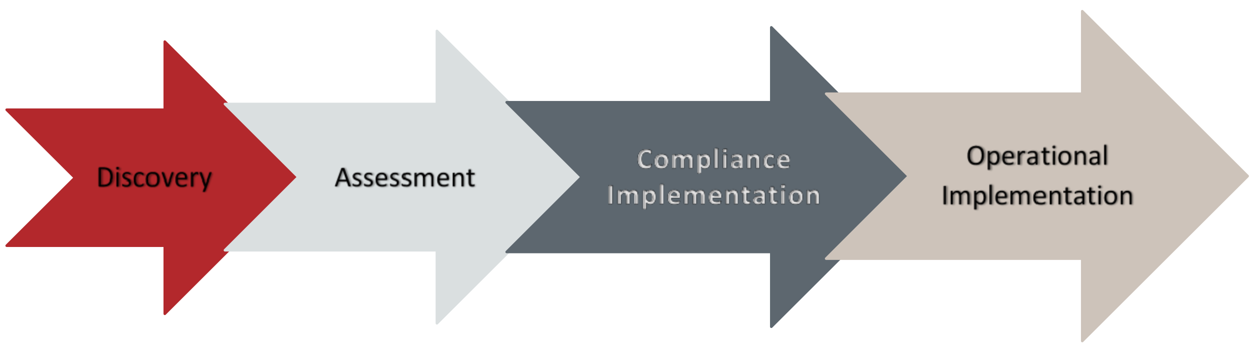
- **Definition of a contract** has expanded. Process and controls must evaluate interactions with the whole of a customer relationship - not just the individual contract or P.O.
- **Termination provisions** are evaluated to determine the contract term which could impact consideration of transaction price and performance obligation.
- **Collectability** assessment is more complex, and the revenue recognition model used when collectability is not probable, could result in delayed revenue recognition (even nonrefundable cash collected may be effected).
- **Contract modifications** are accounted for under a comprehensive model that provides for different outcomes depending on the facts and circumstances.
- **Contract options** are accounted for as separate performance obligations if they provide an incremental benefit that would not have been received without the initial purchase (i.e. “material right”).
- **Multiple-element arrangements:**
    - Revenue allocated to delivered performance obligations must also consider contingent amounts.
    - **Vendor specific objective evidence (VSOE)** of fair value has been eliminated as a separation criterion which may result in the earlier recognition of revenue.
    - Companies must evaluate Contract Promises, likely resulting in additional Performance Obligations.
- **Post contract customer support (PCS)** is not a unique service contemplated or defined in the new standard.
    - Generally includes two separate performance obligations
    - When-and-if unspecified updates
    - Telephone/technical support
- **Significant financing component** guidance is applied to both deferred and advance payments which may result in the recognition of interest income (deferred payment) or interest expense (advanced payment).
- **License renewals** (including in substance renewals) may not be recognized prior to the commencement of the renewal period (a change from legacy GAAP).
- **Licenses** are evaluated to determine whether they include a right to use (point in time) or a right to access (over time) intellectual property.
- **Costs related to customer contracts** (costs to obtain or fulfill a contract) must be capitalized in certain circumstances (i.e. Commissions).
- **Balance sheet presentation** requires separate recognition of contract liabilities, accounts receivable, and contract assets.
- **Disclosure requirements** are significant and likely involve tracking (and disclosing) a variety of information not historically tracked or disclosed.

What is the Impact of ASC606 on CFOs?

Although compliance due dates are rapidly approaching, many organizations are still behind in completing their revenue recognition programs. With the widespread impact across all business units, this slow progress isn't unexpected.

While a revenue recognition compliance program must include members of executive leadership, CFOs will undoubtedly play the leading role to fully transform the business and drive long-term value. Revenue readiness can drive business transformation in critical areas that impact financial reporting, cost reduction, tax efficiencies, data quality, security, audit functionality and more.

The BPM ASC 606 Compliance Journey: We do more than just Account. We Operationalize.



We work closely with CFOs, in companies of all sizes, to help prepare for the transition:

- **Contracts with customers:** We use our technical and operational expertise and apply that to your business and industry as your partner, reducing the time to assess and mitigating business disruption.
- **COGS and operating expenses impacted via ASC340-40:** We can help you manage margin impact and recommend opportunities to minimize the impact going forward.
- **Assess, value and implementation:** Through our comprehensive approach, we reduce distractions and increase efficiencies to keep you focused on your business.
- **ASC 606 requires 50+ controls:** Since financial statement disclosures likely double, we design your implementation to consider these upfront so you're not going back after we leave.
- **ERPs are unprepared, excel files just can't keep up:** We will recommend - and help design - system requirements that meet your operational and business needs. This includes system or module implementations across the entire business - not just the accounting function.
- **Operational implications are complicated and impact the entire organization:**
    - ✓ Debt covenants
    - ✓ KPI's and Investor messaging
    - ✓ Contract management
    - ✓ Compensation planning
    - ✓ Tax planning
    - ✓ Audit readiness

Best Practices

1. **Joint Steering Committee (JSC)**

   - The team is most effective if formed at the onset of a transformation project and should include team leaders from Human Resources, IT, Sales, Marketing, Executive Management and Legal – as well as any 3rd party consultants – (Auditor, Outsourced accounting, IT).

2. **JSC Meetings Timetable**

   - Discovery Phase: At onset, then weekly through the assessment phase.
   - Compliance Implementation Phase: Project delivery team meets weekly (1/2 hour) with larger team meeting bi-weekly (~1/2 hour).
   - Operational Implementation Phase: Project delivery team meets twice a week (1/2 hour or less) with larger team meeting weekly to bi-weekly (depending on complexity of implementation).

3. **Project Management**

   - Designate a project manager at project onset. This person is the hub and is responsible to ensure that all the JSC and / or project delivery team members are being communicated to, heard from, and are “bought-into” the plan. This project manager should not be an internal accounting person.

4. **Create Initial Project Plan – (a must)**

   - Create an initial project plan - working through core deliverables and target due dates.
   - Ensure your team members and JSC members include blocks of time OOO or when they are unavailable. Make concessions for alternates to step in where possible.
   - Determine any stage gates for key deliverable dates (i.e. team member availability, other system implementations, 3rd party consultants, month-end close, budget cycles, holiday shut down’s, etc.).
   - Assign / define all tasks and dependencies. Accountability is Imperative.
   - The Project Plan is a living document and should not be hidden away. SHARE and be Transparent!

5. **Re-Evaluate Project Plan**

   - Project plan should get more granular as the project moves on.
   - JSC meetings should be used to review the Plan, ensure accountability and have a forum for scope, timeline or deliverable changes - not with side meetings.

6. **Execute**

   - You have a strong JSC, a well thought-out Scope of the Project, and a detailed Project Plan. Get to work. Analysis paralysis and overthinking are great ways to miss due dates, create delays, and overcomplicate a project. Keep things simple, check in often, and communicate effectively.

What Are Next Steps?

Through a tailored, automated revenue recognition program, companies can control exposure to risks while reaping the benefits of a strategic approach to business management. Many companies will attempt to manage additional calculations and reports manually. Spreadsheets continue to present more challenges, risks, and inefficiencies. Companies that effectively engage and collaborate cross-functionally, and partner with a strong technical and operational team early in the process, will drive business transformation in critical areas well beyond accounting and reporting – i.e. strategic cost reductions and tax efficiencies, streamlined compensation arrangements, improved contract management processes, increased transparency within business units, and better data quality that provides data-driven insight.

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About BPM

BPM Advisory Practice Group

Don't know where to start? BPM's Advisory Practice is comprised of executive operators (CFOs and Controllers) who collaborate with companies cross-functionally and drive business transformation in critical areas well beyond accounting and reporting. Contact us today.

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