

THE 101 ON 606

NAVIGATING CHANGES TO REVENUE RECOGNITION IN **ASC 606**

[VIEW OUR ASC 606
ONLINE CONTENT](#)

embarc.

SO HERE'S THE DEAL

We know everyone's bombarding you with "rev rec is coming!!!" doomsday messages. A large percentage of CFO's & CAO's are hoping it will just go away. Unfortunately though, it's not going anywhere.

If you've talked it through with your auditors, you probably have an idea of the impact you're expecting. **This is only the beginning**, but you've taken that step at least, and for that we applaud you!

Regardless of where you are at in the process, this guide exists to systematically walk through the process and sift through the mountains of available information.

**WATCH A VIDEO ON WHY
THIS MATTERS**

KEY POINTS

Only one.

✓ **START***



You should have started at least a year ago. So at the very least, start now. Understand the guidance, collaborate with your auditors. Implement new systems and controls. Can't get it right? -- Let us help.

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REV REC RESOURCES

ABOUT EMBARK



WE HEAR IT ALL THE TIME...

When we mention the new revenue changes, we can literally see people check out of the conversation. **“We already looked into that”** or **“ASC606 wont affect us all that much”**. The subject is quickly changed, and heads continue to be buried in the sand.

SO YOU'VE ALREADY LOOKED AT

1 | CONTRACT COST



Capitalize cost to acquire contract, could include sales commissions, fees, etc.

2 | CONTRACT COMBINATIONS



Multiple contracts viewed as one, and modifications.

3 | REVENUE ALLOCATION



Stand-alone sales price, contract term, transaction price, etc.

4 | TRANSACTION PRICE



Estimation of total consideration expected to receive over the contract at initiation. (variable discounts, volume rebates, sales returns, etc.)

AND



You've also applied the 5 step method, documented everything, and made sure that you're on the same page with your auditors.



You've ensured your systems can capture all the newly required information and that you won't need to make any more changes to the process or systems.



You've prepared and vetted your auditor, and all the disclosures that you're going to need for 2016 and beyond.

YOU'RE RIGHT, YOU'RE GOLDEN.

Congratulations, you're in the 1% of public companies that have already made this happen! Now, for most of us in the real world that haven't already gone through the entire process, this breakdown and guide is here to help. You should be able to apply it to where you are in the process and use it to help keep everything on track. Enjoy!



INDUSTRY BREAKDOWN

Not all industries are created equal. And revenue recognition isn't either.

Let's take a look at some items impacted and the relative impact that the new changes will have on various industries, some will experience a higher impact. We know you'll just skip right to your specific industry. We would too. Cheers!

IMPACTED INDUSTRIES



ASSET MANAGEMENT

Estimate performance based fees, up-front fees now deferred. Capitalize cost to acquire contract (sales commissions).



HOSPITALITY

Customer loyalty programs.



MANUFACTURING

Services, products, support, warranty, determine transaction prices.



CONSUMER PRODUCTS & RETAIL

Transaction price and revenue allocation (bounce back coupons (redemption rate), warranties, sales incentives, licenses, loyalty program, or right to return, gift cards, and layaway sales deposits).

HIGHER IMPACT INDUSTRIES



AEROSPACE & DEFENSE

No % completion, recognize revenue at a point in time or over time. Data to support distinct performance obligations within existing contracts. Fulfillment cost recognition.



OIL & GAS

Joint Arrangement, commodity derivatives, and exchange agreements.



TELECOM

Allocation (rev. and transaction price), customer contract modification (frequently added / removed services, combining contracts with customer and reallocating revenues), credit risk.



HEALTHCARE

Expectation to pay, transaction price allocation (government program, insurance, self-pay), bad debt.



REAL ESTATE & CONSTRUCTION

No % completion, recognize revenue at a point in time or over time. Data to support distinct performance obligations within existing contracts, fulfillment cost rec., (capitalize or rec.)



TECHNOLOGY

Software licenses, SaaS, unbundling hosting, software, support, post contract customer service, upgrades.



POWER & UTILITIES

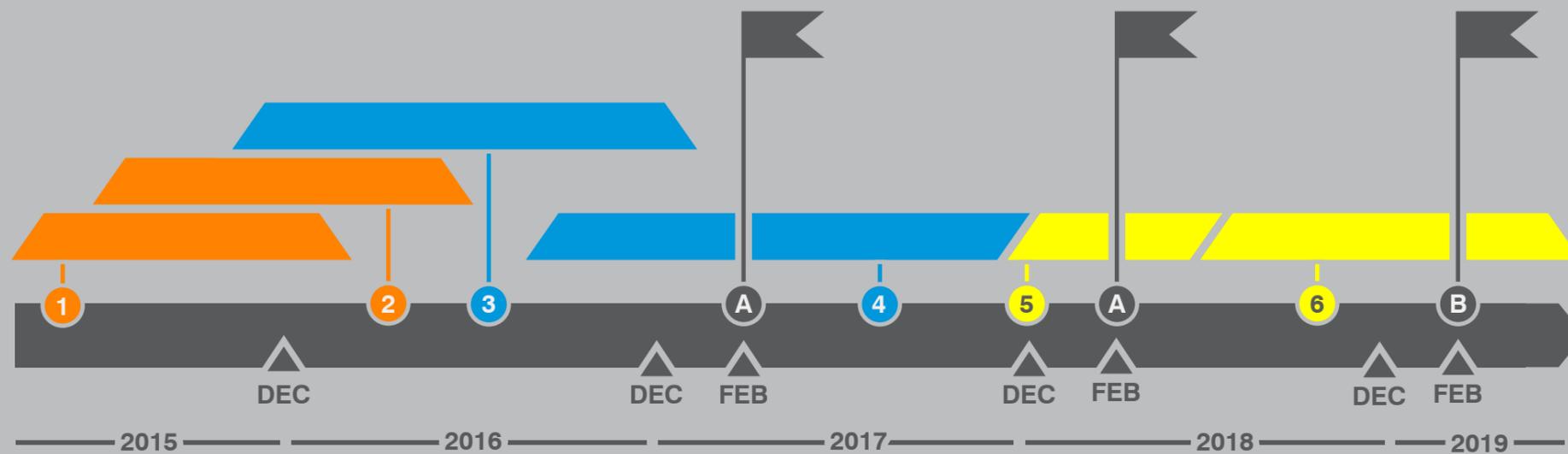
Transaction price - variability driven by cost based structure, index price structure, fixed price structure subject to acceleration / deceleration, unwinding the bundle (allocation base on stand-alone prices).



TIMELINE TO DISCLOSURE

The time to start all of this was a while ago. But we thought it could help us all get on the same page if you could visualize a timeline.

The time is now. It's not going away.



1 PROJECT PLAN

Get everybody onboard, identify process owners, include auditors, set deadlines.

2 EVALUATE REVENUE

Review existing revenue streams and document how they are currently being accounted for.

3 APPLY NEW STANDARD

Go through the 5 steps for each type of revenue.

4 SYSTEMS & CONTROLS

Determine if any control gaps exist under the new standard and if the current systems can accommodate the update.

5 TRAIN & TEST

Train your employees on the new processes and test the updated systems.

6 CONTROLS EFFECTIVE

To continue to obtain maximum control reliance from external auditors, new or revised controls need to be operating effectively throughout the entire year. Otherwise more testing and more fees for your auditors.

A SAB 74 DISCLOSURE

At minimum, provide a qualitative assessment of the new standards impact on the company's financial statements.

B ASC606 DISCLOSURE

February 2019: Provide full disclosure in accordance with the chosen adoption methodology.

LET'S BREAK THIS DOWN

There's a lot to this new regulation and a lot to your timeline to implement. Here's a helpful key.



PREPARATION



IMPLEMENTATION



OPERATION



MILESTONE

WATCH A SHORT VIDEO
ON THIS TIMELINE



AUDITORS NEED FRIENDS TOO

Get comfy with your auditors, you'll be spending some time together. Work with them to create a solution that works for everyone.

-  Have you already talked to them and received their feedback on the potential impact?
-  Do they have specific requests?
-  How would they suggest you proceed?
-  Do they have any guidance on the disclosures or resources you should seek out?

**THEY CAN NOT DO IT FOR YOU,
BUT THEY CAN AND SHOULD HELP.**

DOCUMENT EVERYTHING



Collaborate with external auditors throughout the implementation. Get buy off from Lead Client Service Partner and concurring partner assigned to your audit.



Document the implementation process as you go.



Create a memo documenting the process you used to analyze how ASC 606 will impact your company.

BE SURE TO ADDRESS:

1. How you assessed that all revenue streams and contracts with customers were **analyzed**. Ensure complete population of all revenue streams and contracts.
2. Process for reviewing system impacts and results, to determine if existing systems are capable to adapt to the new guidance.
3. Watch out for any new Information produced by the Entity (IPE), and make sure you have controls in place to address the completeness and accuracy of the IPE.
4. Determine if the existing internal controls continue to mitigate the risks of material misstatement under the new accounting guidance.
5. Which **adoption approach** the company will take.



SELECT AN APPROACH FOR YOUR COMPANY.

The right decision is not always the easiest. Take the time to evaluate your circumstances, talk to your stakeholders, talk to your auditors, talk to your management, and make the best decision for your company... which is not necessarily the path of least resistance.

Here are just some of the pros and cons to consider as you go through this decision process.



FULL RETROSPECTIVE

Restate all years presented under the new standard. This will be 2016, 2017, and 2018.



P&L for all years presented is comparable.



If you expect revenue acceleration, revenue will not be "lost" through an equity adjustment.



Required to restate all contracts outstanding for years presented.



May require significant effort to implement.

MODIFIED RETROSPECTIVE

Record the cumulative impact of the new standard of the two previous years (2016 and 2017) in beginning equity in the current year (2018).



Only outstanding contracts at the transition date need to be restated. i.e. as of year-end 2018



Do not have to restate all years presented, only recognize in equity for current year.



Additional disclosures - have to maintain records in both old and new to disclose the impact on each financial statement line item in the current year and an explanation of the reasons for significant changes.



P&L for all years presented is not comparable and related performance measurements may be skewed



PUT A TEAM TOGETHER

AND A PLAN*

Select a project manager & process owners knowledgeable in:

ASC606

ACCOUNTING SYSTEMS

INTERNAL CONTROLS



Develop project timeline, project plan, and project deliverables.

WHAT DO YOU HAVE NOW?

Now that you've seen the lay of the land, review your current accounting system and internal control requirements. Identify each revenue stream, and do the following for each identified:



DESCRIBE

Describe how revenue is currently recognized in your business



DIAGRAM

Create a process flow displaying how revenue is captured, processed and recorded in the financial statements.



IDENTIFY

Identify internal controls both manual and GITC.

HISTORICAL DATA

Evaluate the availability and retention of historical revenue data. This could include contracts, transaction level detail, and more.

PROJECT PLAN

Update the project plan and resource requirements as needed throughout the process.

REVENUE EXCLUSIONS

[SEE EXCLUSIONS HERE](#)



FIVE STEP MODEL

The new standard has developed a 5 step method to support the core principal: Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

1. IDENTIFY CONTRACT(S) WITH CUSTOMER
2. IDENTIFY PERFORMANCE OBLIGATIONS
3. DETERMINE THE TRANSACTION PRICE
4. ALLOCATE PRICE TO PERFORMANCE OBLIGATIONS
5. RECOGNIZE REVENUE WITH PERFORMANCE

**YOU'VE
DONE X,Y,Z...**

**LET'S DO
THIS!**

While every business and situation is different, the information here is relevant to all industries.

The overall process is complex, but we've summarized the 5 steps of the new regulation in the following slides.

**WATCH A VIDEO OUTLINING
THE FIVE STEPS.**



1. IDENTIFY CONTRACTS WITH CUSTOMER

Do I have a contract? Seems simple, right? Well, it's not.

The criteria that are required to be in place to establish that a contract exists are intended to demonstrate that there is a valid and genuine transaction between an entity and its customer and that the parties to the contract have enforceable rights and obligations that will have true economic consequences.

The rest of the new standard relies on a careful analysis of the enforceable rights and obligations under the contract, if any of the 5 criteria (to the right) are not met, the rest of the revenue recognition model cannot be applied.

LIST

Obtain a complete and accurate list of all arrangements with all customers.

TERM

Determine the contract term for all contracts with customer.

DETERMINE IF YOU HAVE A CONTRACT:

- ✓ **Contract approved and committed to perform by each party**
- ✓ **Identify each party's rights**
- ✓ **Identify the payment terms**
- ✓ **Commercial substance**
- ✓ **Probable collectability**



IDENTIFY EVERYTHING

Identify all material explicit and implicit promised goods or services in the contract.

TO BUNDLE OR NOT?

Determine if a good or service (or a bundle of goods or services) are capable of being distinct. 'Distinct' is a defined paradigm laid out in ASC-606-10-25-20.

SEE DEFINITION OF DISTINCT

If not, combine two or more goods or services and reevaluate the new bundle.

PERFORMANCE OBLIGATIONS

Determine if there is a series of distinct goods or services that result in a single performance obligation.

DEFINE THE NATURE OF THE PROMISE

What has your company promised to the customer? Sometimes this is easy and sometimes its not. The latter often involves critical judgments that your company must make in determining the correct unit of account (i.e., performance obligation).

2. IDENTIFY PERFORMANCE OBLIGATIONS

This is possibly the most important step in the new revenue framework as it establishes the unit of account for revenue recognition.

A miscalculation in this step will quite possibly lead to a material error in the recognition of revenue.

WATCH A VIDEO ON
PERFORMANCE OBLIGATIONS



3. DETERMINE TRANSACTION PRICE

ESTIMATE VARIABLE CONSIDERATION

Determine which method will be used to estimate each type of variable consideration.

EXPECTED VALUE

OR

MOST LIKELY AMOUNT

TRANSACTION PRICE COMPONENTS

Identify each component of the transaction price.

Complexities can arise where a contract includes any of the following:

NON-CASH CONSIDERATION



FIXED CONSIDERATION



VARIABLE CONSIDERATION



CONSIDERATION PAYABLE TO CUSTOMER



SIGNIFICANT FINANCING COMPONENT



Determine the standalone selling price at contract inception of the distinct good or service for each performance obligation in the contract.

ALLOCATE

SELLING PRICE

Allocate the transaction price to performance obligations on a relative standalone selling price basis.

DISCOUNTED

Allocate discounted transaction price proportionately to each distinct good or service on the basis of standalone selling price.

CONSIDERATION

Allocate variable consideration.

Keep in mind changes in transaction price in the future are typically allocated to the performance obligations on the **same basis used at contract inception.**

4. ALLOCATE TRANSACTION PRICE

Now that you know your performance obligations, it's time to allocate the transaction price to each different performance obligation. However, it's never that straight forward.

To the left are some of the highlights of Step 4 and items to consider.

[MORE INFORMATION ON TRANSACTION PRICES](#)



5. RECOGNIZE REVENUE

ASC 606-10-25-23

An entity shall recognize revenue when (or as) the entity satisfies a performance obligation by transferring a promised good or service (that is, an asset) to a customer.

An asset is transferred when (or as) the **customer obtains control of that asset.***



If you cannot conclude that control is transferred over time, control is considered to be transferred at a point in time.

WHEN DOES THE CUSTOMER OBTAIN CONTROL?

Use the five below indicators to determine the point in time at which a customer obtains control (ASC 606-10-25-30).

1. Entity has a present right to payment for the asset.
2. Customer has legal title to the asset.
3. Entity has transferred physical possession of the asset.
4. Customer has the significant risk and rewards of ownership of the asset.
5. Customer has accepted the asset.

[READ MORE ON ASSET CONTROL](#)



WHAT COMES AFTER FIVE?

Looking ahead to the future, you've got smooth sailing but haven't yet reached land.

[WATCH VIDEO ON LOOKING
AHEAD TO THE FUTURE](#)



SYSTEMS & CONTROLS

Systems and controls work hand in hand to bring you into compliance and keep you in compliance.

They also mitigate risks throughout your company, and an effective control environment can limit the fees of your external auditor.

**MORE INFORMATION ON
SYSTEMS & CONTROLS**

SYSTEMS

1. Evaluate and document the accounting system requirements for the new revenue process
2. Create a flowchart documenting the new revenue recognition process for each revenue stream
3. Evaluate where and how the accounting system(s) needs to change
4. Work with the designated IT team to develop a plan and timeline to implement system changes

CONTROLS

1. Evaluate and document the internal controls requirements for the new revenue process
2. Create a flowchart documenting the new revenue recognition process for each revenue stream
3. Determine if there are any gaps in internal controls including any new Information Used in the Control (IUC)

SYSTEMS & CONTROLS

1. Develop training materials and train all staff on new accounting processes and controls
2. Execute the plan and test the results by 12/31/2017 to maximize effectiveness and return on investment



LOOKING AHEAD

The SEC's expectation is that disclosure increases in explanation and specificity as the transition date approaches.

MORE ON SAB TOPIC 11.M (SAB 74)

AND IF THAT DOESN'T WORK...

If a registrant is unable to reasonably estimate the impact of adopting this standard, the registrant should consider the following additional qualitative disclosures in regards to the significance of the impact on its financial statements.

ADDITIONAL QUALITATIVE DISCLOSURES:

EFFECTS

The effect of any accounting policies resulting from the adoption of the new standard.

DIFFERENCES

How the new policies differ from current ones.

STATUS

The status of the implementation process and nature of any significant matters that have not yet been addressed.

NOW FOR THE NOW

So the SEC just came out with their expectations for the disclosures they want to see on your 10K in ~~a few months~~ a few weeks, for fiscal year 2016 and beyond.

You know that and already have it taken care of, **right?**



"YOUR 2018 DISCLOSURE", AKA THE FUTURE

After 2017 the real disclosures and changes come into play. Here's what to expect.

ASC 606-10-50-1

The objective of ASC 606-10-50-1 is to disclose sufficient information to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers.

AN ENTITY SHALL DISCLOSE:

CONTRACTS

Revenue recognized from contracts with customers

JUDGEMENTS

The significant judgments, and changes in the judgments, made in applying the guidance in this topic to those contracts

ASSETS

Any assets recognized from the costs to obtain or fulfill a contract with a customer in accordance with ASC 606-10-50-1



REVENUE RECOGNITION RESOURCES

SAY THAT FOUR TIMES, FAST.

The big four have put out a veritable mountain of information on the topic. This is overwhelming to even experts, which is why we have made our online resources as approachable as possible.

OUR ONLINE RESOURCES

ASC 606 DOCUMENTATION:
DELOITTE (468 PAGES)

ASC 606 DOCUMENTATION:
EY (685 PAGES)

ASC 606 DOCUMENTATION:
PwC (541 PAGES)

(HUMAN) RESOURCES

MEET SOME OF US



CLANCY FOSSUM
CPA, COO

13+ years at Deloitte, IPO experience, Texas Tech Alumni

While I'm not at work, I spend my time with my wife and our four kids. We're either on the golf course, playing some sort of competition in our backyard, or arguing over who's changing the next diaper.



JAMES DURRENBERGER
CPA, DIRECTOR

10+ years of Big 4 & corporate experience, PwC Alumni, University of Texas Alumni

I spend time with my family and I usually have a camera in hand. I have been known to build things around the house (including a manual Polaroid camera affectionately named "The Franken-roid") and do remodeling projects from time to time.

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11+ years of Big 4 & corporate experience, EY Alumni, OSU Alumni

When I'm not using my trusty 10-key, you can find me training for half marathons, playing with my niece and nephew, or traveling the US and abroad.



SAM WU
CPA, MANAGER

5+ years of public & corporate experience, GT Alumni, University of Texas Alumni

I enjoy making brisket and spending time giving back to the community at Solomon's Porch, a downtown homeless ministry. I also love all things CrossFit, especially Olympic lifting, and I hope to be competitive one day.



embark.

WHO WE ARE

As a group of CPAs with both Big 4 public accounting and industry experience, we can do a lot. Literally. We're not only former auditors and we're not your tax experts.

Instead, we can help your team in a ton of ways – taking the time to listen closely, helping identify challenges and finding areas prime for your improvement and growth.

To bright financial professionals seeking smart solutions, Embark is the boutique consulting partner that strengthens businesses by building close personal and professional relationships.

VALUES



DISRUPTOR

The "reasonable" person accepts life the way it is. We believe in being unreasonable and disrupting "how things have always been done" because it helps us identify ways we can change, grow and improve.



RELATIONSHIPS

Everything we do depends on our ability to build real relationships. If we fail, our clients' phones will ring very, very quickly. Let's keep them quiet.



STRATEGIC

Most people get by in their day-to-day jobs without thinking deeply about problems. We don't want robots; we want critically thinking, agile-minded rockstars at all levels of our team. Makes sense right?!



WITTY

There's a certain "je ne sais quoi" or "edge" about our people that's hard to pinpoint. Sure, we're mostly accountants but we like to think we're the fun ones!



INTELLIGENT

We don't have the luxury of "not getting it" in our business. So the ability to quickly pick-up, organize, and use new information in unique environments is critical to successfully serve clients. We MUST hire the "wicked smart kids" and let them loose!



CLUTCH

Here's the thing: stuff happens. And when it does, lives are affected. We get that, and our team is there to help you when you need us. We'll come through when others drop the ball. Can your business afford to let deadlines pass or opportunities vanish? Ours can't.



