Revenue Recognition Overview

Cherry Bekaert LLP
CPAs & Advisors

5-Step Process

Identify Contract(s) with Customer

Requirements for a contract

- Parties have agreed and are committed to perform.
- Identify each party's rights.
- Identify payment terms.
- Commercial Substance.
- Probability entity will collect consideration to which it is entitled.

Contract modifications treated as:

- **Separate contract** – If goods are distinct and at their stand-alone selling price.
- **Modification** – Treated as termination of original contract, additional goods services combined with undelivered (if distinct) or delivered and undelivered (if not distinct) elements of original as if one contract.

Identify Performance Obligation(s) in Contract

Identify promised goods and services, then identify performance obligations as either:

- Goods/services that are distinct.
- Series of distinct goods/services that are the same or have the same pattern of transfer and can be satisfied over time.

Is it distinct?

- Can customer benefit from it by itself or together with readily available resources?
- Is it distinct in the context of the contract (e.g., providing electrical or building you a house)?

Determine Contract Price

Estimating variable consideration

- **The expected value** – Sum of probability weighted amounts in a range of possible amounts.
- **The most likely amount** – Single most likely amount in a range of possible amounts. Typically used when only two possible outcomes.
- **Constraint (or limit) to calculation above** – Amount probable (70-80%) not to reverse.

Non-cash and other considerations:

- Financing component >1 year
- Volume discounts
- Rebates
- Variable pricing based on other external factors

Allocate Transaction Price to Performance Obligation(s)

Best evidence is the stand-alone selling price the entity charges. Other methods include:

- **Adjusted market approach** – Consider market place/ conditions, profit margin.
- **Expected cost & margin** – Consider margins on similar products, historical evidence.
- **Residual approach (least desirable)** – Only may be used if:
  - Entity sells same good or service for a broad range of amounts, or
  - Good or service has not been sold previously on stand-alone basis.

Note: Variable consideration might be allocated to one or more performance obligations.

Recognize Revenue When Entity Satisfies Performance Obligation(s)

Recognize revenue when the entity satisfies a performance obligation by transferring "control" of good or service to a customer.

Recognize revenue either point in time or over time:

- **Point in time** – Recognize when control transferred to customer. Five indicators:
  - Entity has right to payment.
  - Customer has legal title.
  - Customer has physical possession.
  - Customer has risks/rewards or ownership.
  - Customer has accepted the good or service.
- **Over time** – Recognize revenue over time if one of the following criteria is met:
  - Customer simultaneously receives and consumes benefits (e.g., cleaning service).
  - Entity creates or enhances asset that the customer controls.

Measuring progress methods:

- **Output methods** – Based on value transferred (e.g., units produced, units delivered).
- **Input methods** – Based on entity's efforts (e.g., cost incurred, labor hours, machine hours).

Management must select method that best depicts a transfer of good or service, not discretionary.

Effective Dates

Public:

Years beginning after December 15, 2017

Non-Public:

Years beginning after December 15, 2018

Scope Exclusion

- Leases
- Contracts under ASC 944
- Financial instruments
- Collaborative arrangements with non-customers

Transition Methods

- **Full Retrospective** – Restate prior years presented
- **Modified Retrospective** – Adjustment to retained earnings in year of adoption (requires disclosure comparing current year under current vs. legacy GAAP)

Note: Many practical expedients for adoption.

Licenses *(intellectual property or IP)*

Right to Access IP

Recognize revenue over time.

Right to Use IP (i.e., as it currently exists)

Recognize revenue at a point in time.

Two types of IP:

- **IP with stand-alone functionality** – You can utilize it right away (e.g., software, films and records). Generally right to use IP.
- **Symbolic IP** – Needs to be combined with other goods or services (e.g., brands and tradenames). Obligation to maintain the value is implied. Generally right to access IP.

Presentation and Disclosure

No more boilerplate footnote disclosures; must include (not all inclusive list):

- Nature, amount, timing and uncertainty of revenue.
- Disaggregates and how affected by economic factors.
- Opening/closing balances of receivables, contract assets and liabilities.
- Information about timing of payments and revenue recognition.
- Judgments and changes in judgments.

Note: Practical expedients exist for non-public entities.

Let us be your guide forward

Michael Hoose, CPA
Sr. Manager, Assurance Services
mhoose@cbh.com

Chase Wright, CPA
Partner, Assurance Services
cwright@cbh.com

Roy Amler, CPA, CMA
Partner, Assurance Services
ramler@cbh.com