

# ASC 606 IMPLEMENTATION IS HERE

## ASC 606: 5 BEST PRACTICES

### Revenue Recognition Accounting Standard

The time has come for private companies to implement one of the Financial Accounting Standard Board's most comprehensive accounting changes in the past two decades. ASC 606 – Revenue from Contracts with Customers was issued over 5 years ago in May 2014 and is now required to be implemented for all privately held companies for the year ending December 31, 2019. We all know change is tough, so what can you and your company do to be ready for ASC 606 implementation?

The following are some best practices to consider when assessing some of the more difficult areas of this new standard:

**1** What is your definition of a performance obligation, how are they identified and ultimately satisfied in order to be entitled to recognize revenue. This will be an important concept that needs to be applied consistently, and this definition will find its way into your GAAP financial statement footnotes. Best practice would be for management to break all revenue streams into performance obligations and determine how and when each of those are satisfied.

**2** Identification of any variable consideration included in any revenue stream. Consideration is variable if the amount an entity will receive is contingent on a future event occurring or not occurring, even though the amount itself is fixed. There's a long list of examples within the principles, such as discounts, credits, rebates, price protection, return rights, price concessions, penalties, performance bonuses, milestones, profit sharing arrangements or royalties. This area contains the most significant estimates and judgements found in the new principles and having documentation that describes the basis for how these judgements are made is a necessity, especially if your company prepares a GAAP financial statement that is compiled, reviewed or audited by a third party accountant or accounting firm.

Best practice would be identifying all potential types of consideration that could potentially occur within your company's revenue recognition model, and then assessing the impact of each variable consideration item.

**3** Have an open dialogue with the sales/marketing teams. It is important to know what kind of variable consideration/incentive offerings may be made by the sales team to customers. The salesperson might be doing everything they can to make a sale, without thinking of what the consequences might be for the accounting department. Best practice would be to compile a list of all potential customer incentives, and make sure sales people are not deviating from those incentive options. Companies that have had loose controls over this part of the contracting process have struggled to implement the new standard because of those inconsistencies. Know what incentives your Company is offering customers and what the proper accounting for those incentives is under the new framework.

**4** Inventory or track your contracts with customers. If your company has a significant volume of contracts with customers, it will be important to inventory those contracts to know what your total potential population to assess for compliance with ASC 606 could be. The new standard implementation not only requires contracts at December 31, 2019 to be in compliance, but at a minimum, any open contract at December 31, 2018 will also need to be analyzed for compliance with ASC 606 which could result in a potential opening equity adjustment under the modified retrospective implementation method. The modified retrospective method has been the more popular implementation choice since it only requires an analysis of open contracts as of December 31, 2018, as the alternative option known as the full retrospective method requires all contracts to comply with ASC 606 for all years presented in the GAAP financial statement, which typically requires much more effort in gathering and analyzing data covering a full two year period.



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Consider using a standard contract. Companies who have determined that using the customers contract as opposed to their own standard contract have struggled to implement. The standard requires a contract by contract assessment, so if each contract is significantly different, it could result in a substantial amount of time analyzing those contracts within the framework. Best practice would be to work towards using standardized contract, or at least negotiating similar terms within your customers' contracts to make the accounting easier.

#### Best Practices

The best practices above will allow you to more efficiently analyze your compliance with ASC 606, and will make any year end interaction with your accountant much easier, as the items listed above are some of the most scrutinized parts of implementation by anyone who is auditing, reviewing or preparing your year end financial statements under generally accepted accounting principles (GAAP). The time for implementation of ASC 606 is now. Are you ready?

#### How Herbein + Company Can Help

Herbein + Company, Inc. is positioned to help our clients work through how this standard will impact their financial position and overall accounting environment, but please understand that we are limited by our independence rules.

For additional information or to contact our team directly email us at [info@herbein.com](mailto:info@herbein.com).

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