

PROTIVITI FLASH REPORT

It's Here, Are You Ready? – Transitioning to the New Revenue Recognition Standard

June 2, 2014

The long-awaited new Financial Accounting Standards Board (FASB) Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers*, was finally issued on May 28, 2014.¹ This new guidance is the result of a collaborative effort by the FASB and the International Accounting Standards Board (IASB) to agree on a global standard based on common principles that can be applied across industries and regions.² In the United States, this new guidance will replace most of the industry-specific Generally Accepted Accounting Principles (GAAP) requirements that have become complex and cumbersome to apply in practice. For the rest of the world, it will replace the IFRS standards for revenue recognition that provide limited implementation guidance and can be difficult to understand and apply.

The new standard is expected to be effective for public entities for fiscal years, including interim periods within those years, beginning after December 15, 2016. For nonpublic entities, the standard is expected to be effective for fiscal years beginning after December 15, 2017, and interim periods thereafter (although nonpublic entities may adopt at the same time as public entities). It affects any entity that enters into contracts with customers unless those contracts are in the scope of other FASB standards (for example, insurance contracts or lease contracts – and lease accounting is the subject of the next expected converged standard).

Why Change? – Objectives and Benefits

Current revenue recognition guidance under U.S. GAAP has developed over a long period of time and consists of myriad disparate requirements for specific transactions and industries – including, for example, software, real estate and construction contracts. Prior to the issuance of the new standard, over 200 specialized and/or industry-specific revenue recognition requirements could be found in the accounting literature under U.S. GAAP. Despite this overwhelming volume of requirements, new and emerging transactions sometimes lack explicit guidance. Therefore, differences in reporting may arise as a result of inconsistencies and weaknesses in the literature. All of these disparate revenue recognition requirements have been superseded by the new standard.

The FASB's new standard includes improved revenue recognition guidance that provides a more robust framework for addressing revenue issues as they arise. This framework is intended to remove the inconsistencies, complexities and burdens in the existing literature, thereby

¹ The new standard is Topic 606 in FASB's Accounting Standards Codification.

² The IASB issued IFRS 15, which is effective for reporting periods beginning on or after January 1, 2017, with earlier application permitted.

increasing comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets. In addition, the new standard requires more disclosure so that investors and other users of financial statements better understand the economics behind the numbers. For preparers, the new standard is intended to simplify the preparation of financial statements by reducing the number of requirements to which an organization must refer.

Several areas were not addressed by the new standard because there are other FASB projects addressing them. These areas include lessor revenue, insurance premium revenue and revenue from certain financial instruments.

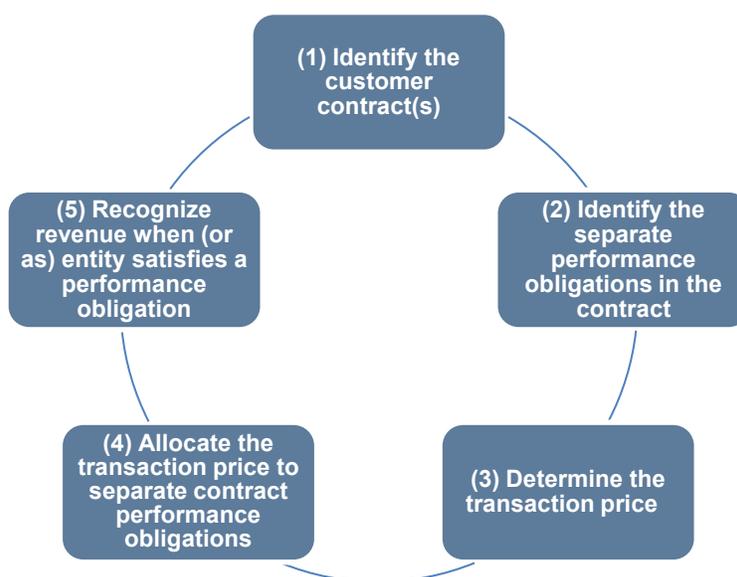
What's New?

Every accounting student ultimately learns that revenue recognition is one of the most important, if not THE most important, accounting policy and practice in preparing financial statements. Revenue is an important number to investors and users of financial statements in assessing a company's performance and prospects for continuing success. In providing guidance, the objective of the new standard is to establish the principles to report useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue from customer contracts.

To meet this objective, the new guidance establishes a new core principle:

Recognize revenue in a manner that depicts 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.

In applying this principle, it is the collective view of the FASB and the IASB that consistent application of the standard will be achieved through the use of a contract-based model, where revenue recognition is based on changes in "contract assets and liabilities." In other words, most, if not all, revenue-generating arrangements are, in effect, contractual arrangements of some form between two parties. Therefore, revenue would be earned and recognized as the reporting organization satisfies performance obligations or promises within this contractual arrangement. Timing of revenue recognition may vary depending on whether the contract is for the delivery of goods or for the performance of a service. To this end, the following five steps should be taken to achieve the core principle outlined in the standard.



These five steps are discussed further below (see “Applications of the Five Steps”). In essence, to achieve the core principle, issuers will evaluate their contracts and commitments to customers to identify the performance obligations, the delivery or satisfaction of those performance obligations, and the consideration they receive from their customers. This will ultimately drive the value and timing of revenue to be reflected in their financial statements.

The basic changes resulting from the new standard and the application of the five steps are summarized below:

- As stated earlier, there will be consistent principles for recognizing revenue, regardless of industry and/or geography, to replace the numerous requirements for recognizing revenue.
- Organizations will be required to disclose quantitative information about contracts with customers, including disaggregation of revenue, contract balances and changes in those balances, remaining performance obligations, and information about assets recognized from the costs to obtain or fulfill contracts with customers; and qualitative information about revenue contracts, including significant judgments involved in applying the revenue guidance. Other than disclosures in accounting policies and segment reporting, most companies provide limited information about revenue contracts.
- Reporting organizations will be required to assess the goods or services promised to a customer, identify performance obligations on the basis of whether the goods or services are distinct, and recognize revenue when (or as) each performance obligation is satisfied. Under prior requirements, many goods or services promised in a contract with a customer are deemed not to be distinct revenue-generating transactions when, in fact, those promises might represent separate obligations of the entity to the customer.
- Companies will be required to allocate the transaction price to each performance obligation (or distinct good or service) in an amount that depicts the amount of consideration to which the entity expects to be entitled in exchange for transferring the promised goods or services to the customer. Under prior requirements, in a multiple element arrangement, the amount of consideration allocated to a delivered element is limited to the amount that is not contingent on delivering future goods or services.
- Variable consideration will be included in the transaction price to the extent it is probable that a significant revenue reversal will not occur. Consideration can vary because of discounts, rebates, refunds, credits, price concessions, incentives, performance bonuses, penalties, or other similar items. Under prior standards, accounting for variable consideration differs greatly across industries.

These are fairly significant changes, requiring a thorough understanding of the economics underlying the various contracts an organization enters into with its customers, identification of the data required to support revenue recognition for the company’s customer contracts and the sources of that data, and modifications of policies, processes and systems to obtain and apply the data in accordance with the requirements of the new standard.

Transition Alternatives

Companies have **two alternatives** when transitioning to the new standard:

- (1) **Retrospective application to each prior reporting period presented** – In applying this alternative, any of the following optional practical expedients may be selected to simplify the transition:

- For completed contracts, an entity need not restate contracts that begin and end within the same annual reporting period.
- For completed contracts that have variable consideration, an entity may use the transaction price at the date the contract was completed rather than estimating variable consideration amounts in the comparative reporting periods.
- For all reporting periods presented before the date of initial application, an entity is not required to disclose the amount of the transaction price allocated to remaining performance obligations nor provide an explanation of when the entity expects to recognize that amount as revenue.

(2) **Cumulative effect reporting in the year of adoption** – In this approach, the cumulative effect of initially adopting the new standard is recognized as an adjustment to the opening balance of retained earnings in the year of initial application. In electing this transition method, the organization should provide the following additional disclosures in reporting periods that include the date of initial application:

- The amount by which each financial statement line item is affected in the current reporting period by the application of the new standard as compared to the revenue recognition guidance that was in effect before the change.
- An explanation of the reasons for any significant changes between the new revenue standard and the legacy revenue recognition policy.

In effect, the difference between these two methods is that the first would require restatement of comparative years and the second would not.

Application of the Five Steps

Step 1: Identify the customer contract(s) – A contract is an agreement between two or more parties that creates enforceable rights and obligations. Contracts can be written, oral or implied by an entity’s customary business practices. The new standard requires application of the proposed revenue guidance to each contract with a customer unless specified criteria are met for the combination of contracts. To illustrate the combination of contracts concept, the entity combines two or more contracts entered into at or near the same time with the same customer (or with related parties) and accounts for the contracts as a single contract if one or more of the following criteria are met:

- The contracts are negotiated as a package with a single commercial objective.
- The amount of consideration to be paid in one contract depends on the price or performance of the other contract.
- The goods or services promised in the contracts (or some goods or services promised in the contracts) are a single performance obligation.

Step 2: Identify the separate performance obligations in the contract – A performance obligation is a promise in a contract with a customer to transfer a good or service to the customer. If an entity promises to transfer more than one good or service, the entity would account for each promised good or service as a separate performance obligation only if it is distinct. If a promised good or service is not distinct, an entity would combine that good or service with other promised goods or services until the entity identifies a bundle of goods or services that is distinct. In some cases, that would result in an entity accounting for all the goods or services promised in a contract as a single performance obligation.

A good or service is distinct if either of the following criteria is met:

- The entity regularly sells the good or service separately.
- The customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer.

Notwithstanding the above criteria, a good or service in a bundle of promised goods or services is not distinct and, therefore, the entity would account for the bundle as a single performance obligation, if both of the following criteria are met:

- The goods or services in the bundle are highly interrelated and transferring them to the customer requires that the entity also provide a significant service of integrating the goods or services into the combined item(s) for which the customer has contracted.
- The bundle of goods or services is significantly modified or customized to fulfill the contract.

The proposed guidance also includes implementation guidance to help an entity to appropriately identify the performance obligations in specified situations. One example is when other parties are involved in providing goods to an entity's customer and the entity must determine whether its performance obligation is to provide the goods by acting as a principal, or to provide the service of arranging for another party to provide the goods by acting as an agent.

The following examples illustrate the identification of performance obligations:

- Assume Company A licenses software to a customer and promises to provide consulting services to significantly customize the software to the customer's technology environment for a total consideration of \$750,000. The license and the consulting represent goods and services. Company A is providing a significant service of integrating these goods and services into the combined item for which the customer has contracted. In addition, the software is significantly customized by the entity in accordance with the specifications negotiated with the customer. Hence, the entity would account for the license and consulting services together as a single performance obligation.
- Assume Company X enters into a contract to design and build an office building. Company X is responsible for the overall management of the project and identifies various goods and services to be provided, including engineering, site clearance, foundation, procurement, construction of the structure, piping and wiring, installation of equipment, and finishing. This bundle of goods and services is a single performance obligation because the goods or services included in the bundle are highly interrelated and providing them to the customer requires the entity also to provide a significant service of integrating the goods or services into the combined item (the construction of the building) for which the customer has contracted. In addition, Company X must modify and customize the goods or services significantly to fulfill the contract.

Step 3: Determine the transaction price – The transaction price is the amount of consideration an entity expects to receive in exchange for transferring promised goods or services to a customer, excluding any amounts collected on behalf of third parties (for example, sales taxes). When determining the transaction price, an entity would consider the effects of all of the following:

- **Variable consideration:** If the promised amount of consideration in a contract is variable, an entity would estimate the transaction price by using either the expected value (that is, probability-weighted amount) or the most likely amount, depending on which method the entity expects to better predict the amount of consideration to which it will be entitled.

- **The time value of money:** An entity would adjust the promised amount of consideration to reflect the time value of money if the contract has a financing component that is significant to the contract. An entity would consider various factors in assessing whether a financing component is significant to a contract. As a practical expedient, an entity need not adjust the promised amount of consideration to reflect the time value of money if the entity expects at contract inception that the period between payment by the customer and the transfer of the promised goods or services to the customer will be one year or less.
- **Noncash consideration:** If a customer promises consideration in a form other than cash, an entity would measure the noncash consideration (or promise of noncash consideration) at fair value. If an entity cannot reasonably estimate the fair value of the noncash consideration, it would measure the consideration indirectly by reference to the standalone selling price of the goods or services promised to the customer in exchange for the consideration.
- **Consideration payable to the customer:** If an entity pays, or expects to pay, consideration to a customer (or to other parties that purchase the entity's goods or services from the customer) in the form of cash, credit, or other items that the customer can apply against amounts owed to the entity, the entity would account for the consideration payable to the customer as a reduction of the transaction price unless the payment is in exchange for a distinct good or service.

An entity would not consider the effects of customer credit risk (that is, collectability) when determining the transaction price but, instead, would account for those effects by applying other guidance.³ Any corresponding amounts recognized in profit or loss (for changes in the allowance for doubtful accounts, loan losses, etc.) would be presented both initially and subsequently as a separate line item adjacent to reported revenues (most often in practice, this reporting will be below the revenue line).

Step 4: Allocate the transaction price to separate performance obligations in the contract

– For a contract that has more than one separate performance obligation, an entity must allocate the transaction price to each separate performance obligation in an amount that reflects the consideration to which the entity would expect to receive in exchange for each separate performance obligation.

To allocate an appropriate amount of consideration to each separate performance obligation, an entity would determine the standalone selling price at contract inception of the good or service underlying each separate performance obligation and allocate the transaction price on a relative standalone selling price basis. If a standalone selling price is not observable, an entity would estimate it. For example, the entity may evaluate the market in which it sells goods or services and estimate the price that customers in that market would be willing to pay for those goods or services, i.e., an adjusted market assessment approach. Another approach an entity may take is to forecast its expected costs of satisfying a performance obligation and then add an appropriate margin for that good or service, i.e., an expected cost plus margin approach. Still another approach may be used whereby an entity may estimate the standalone selling price by reference to the total transaction price less the sum of the observable standalone selling prices of other goods or services promised in the contract, i.e., a residual approach. This latter

³ For example, see FASB Financial Accounting Series, *Receivables (Topic 310)*, or IFRS 9, *Financial Instruments*.

approach may be useful if the standalone selling price of a good or service is highly variable⁴ or uncertain.⁵

The proposed guidance specifies the circumstances in which an entity would allocate a discount or a contingent amount entirely to one (or some) distinct goods or services promised in a contract rather than to all promised goods or services in the contract. For example, an entity shall allocate a discount entirely to one (or some) separate performance obligation(s) in the contract if both of the following criteria are met:

- The entity regularly sells each good or service (or each bundle of goods or services) in the contract on a standalone basis.
- The observable selling prices from those standalone sales provide evidence of the performance obligation(s) to which the entire discount in the contract belongs.

If the transaction price includes an amount of consideration that is contingent on a future event or circumstance (for example, an entity's performance or a specific outcome of the entity's performance), the entity shall allocate that contingent amount (and subsequent changes to the amount) entirely to a distinct good or service if both of the following criteria are met:

- The contingent payment terms for the distinct good or service relate specifically to the entity's efforts to transfer that good or service (or to a specific outcome from transferring that good or service).
- Allocating the contingent amount of consideration entirely to the distinct good or service is consistent with the standard's allocation principle⁶ when considering all of the performance obligations and payment terms in the contract.

An entity would allocate to the separate performance obligations in a contract any subsequent changes in the transaction price on the same basis as at contract inception. Amounts allocated to a satisfied performance obligation would be recognized as revenue, or as a reduction of revenue, in the period in which the transaction price changes.

Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation – An entity would recognize revenue when (or as) it satisfies a performance obligation by transferring a promised good or service to a customer. A good or service is transferred when (or as) the customer obtains control of that good or service.

For each separate performance obligation, an entity would determine whether the entity satisfies the performance obligation over time by transferring control of a good or service over time. If the entity does not satisfy a performance obligation over time, the performance obligation is satisfied at a point in time. To determine the point in time when a customer obtains control of a promised asset and an entity satisfies a performance obligation, the entity would consider indicators of the transfer of control that include, but are not limited to, the following:

- The entity has a present right to payment for the asset.
- The customer has legal title to the asset.

⁴ A selling price is highly variable when an entity sells the same good or service to different customers (at or near the same time) for a broad range of amounts.

⁵ A selling price is uncertain when an entity has not yet established a price for a good or service and the good or service has not previously been sold.

⁶ The standard's allocation principle (Step 4) provides that the transaction price to each separate performance obligation in an amount that depicts the amount of consideration to which the entity expects to be entitled in exchange for satisfying each separate performance obligation.

- The entity has transferred physical possession of the asset.
- The customer has the significant risks and rewards of ownership of the asset.
- The customer has accepted the asset.

To help an entity determine when control of a promised good or service is transferred to a customer, the standard includes implementation guidance on specified topics such as repurchase agreements, consignment arrangements and bill-and-hold arrangements.

When an entity transfers control of a good or service over time and, hence, satisfies a performance obligation over time, it recognizes revenue over time if at least one of the following two criteria is met:

- (1) The entity's performance creates or enhances an asset (for example, work in process) that the customer controls as the asset is created or enhanced.
- (2) The entity's performance does not create an asset with an alternative use to the entity and at least one of the following criteria is met:
 - The customer simultaneously receives and consumes the benefits of the entity's performance as the entity performs.
 - Another entity would not need to substantially reperform the work the entity has completed to date, if that other entity were to fulfill the remaining obligation to the customer.
 - The entity has a right to payment for performance completed to date and it expects to fulfill the contract as promised.

For each separate performance obligation that an entity satisfies over time, the entity would recognize revenue over time by consistently applying a method of measuring the progress toward complete satisfaction of that performance obligation. Appropriate methods of measuring progress include so-called "output methods" and "input methods." Output methods recognize revenue on the basis of direct measures of the value delivered to the customer in the form of goods and/or services transferred to date. They include surveys of performance completed to date, appraisals of results achieved, milestones reached, or units produced. If an entity has a right to invoice a customer in an amount that corresponds directly with the value to the customer of the entity's performance completed to date (for example, a services contract in which an entity bills a fixed amount for each hour of service provided), the entity shall recognize revenue in the amount to which the entity has a right to invoice.

Input methods recognize revenue on the basis of the entity's efforts or inputs to the satisfaction of a performance obligation (for example, resources consumed, labor hours expended, costs incurred, time lapsed, or machine hours used) relative to the total expected inputs to the satisfaction of that performance obligation. For example, if the entity's efforts or inputs are expended evenly throughout the performance period, it may be appropriate for an entity to recognize revenue on a straight-line basis.

Input methods may be used when outputs are not directly observable or the information required to apply an output method may not be available to the entity without undue cost. One issue with input methods is that there may not be a direct relationship between the entity's inputs and the transfer of control of goods or services to the customer because of inefficiencies in the entity's performance or other factors. Hence, when using an input method, an entity shall exclude the effects of any inputs that do not depict the transfer of control of goods or services to the customer. To illustrate, the costs of wasted materials, labor or other resources to fulfill the

contract that were not reflected in the price of the contract should not be considered when applying an input method.

When applying an input method to a separate performance obligation that includes goods that the customer obtains control of significantly before receiving services related to those goods, the best depiction of the entity's performance may be for the entity to recognize revenue for the transferred goods in an amount equal to the costs of those goods if both of the following conditions are present at contract inception:

- The cost of the transferred goods is significant relative to the total expected costs to completely satisfy the performance obligation.
- The entity procures the goods from another entity and is not significantly involved in designing and manufacturing the goods

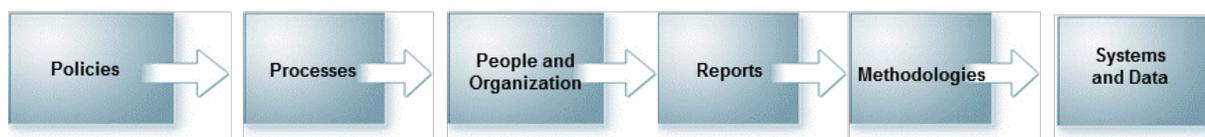
As circumstances change over time, an entity would update the measurable indicators of progress and performance towards completion. An entity shall recognize revenue for a performance obligation satisfied over time only if the entity can reasonably measure its progress toward complete satisfaction of the performance obligation. An entity would not be able to meet this requirement (i.e., reasonably measure its progress toward complete satisfaction of a performance obligation) if it lacks reliable information necessary to apply an appropriate output or input measurement method.

In some circumstances (for example, in the early stages of a contract), an entity may not be able to reasonably measure the outcome of a performance obligation, but still expects to recover the costs incurred in satisfying the performance obligation. In those circumstances, the entity shall recognize revenue only to the extent of the costs incurred until such time that it can reasonably measure the outcome of the performance obligation or until the performance obligation becomes onerous.⁷

Points to Consider

Now that the end game of revenue recognition convergence is clearer, organizations should take steps now to consider appropriate changes related to policies, people, processes and technology. The standard setters' efforts to codify revenue recognition principles that apply to all industries have resulted in changes in nomenclature that will require careful consideration. The longest standard the FASB has ever issued, the new revenue recognition guidance will challenge even the most experienced of financial statement preparers.

In planning to adopt the new revenue standard, companies would benefit from considering the six elements of infrastructure – starting from policies and processes all the way to systems and data.



⁷ A performance obligation is “onerous” if the lowest cost of settling the performance obligation exceeds the amount of the transaction price allocated to that performance obligation. The lowest cost of settling a performance obligation is the lower of: (a) the costs that relate directly to satisfying the performance obligation by transferring the promised goods or services (e.g., direct labor, direct materials, allocations of costs that relate directly to the contract or to contract activities, costs that are explicitly chargeable to the customer under the contract, and other costs that are incurred only because the entity entered into the contract), or (b) the amount that the entity would pay to exit the performance obligation if the entity is permitted to do so other than by transferring the promised goods or services.

In particular, organizations should examine their processes and systems around the order-to-cash cycle data requirements and revenue recognition reporting, and make certain that data flowing from transaction reporting to financial reporting is accurate and complete. Long-term projects, such as system changes and employee education, will be unavoidable for U.S. firms that must adapt to the revenue standard convergence and require early planning to be successful and cost-efficient.

While no industry will be totally exempt, industries that are likely to experience the most significant changes include software, telecommunications, asset management, airlines, real estate, aerospace and construction. Changes won't be limited to these industries, of course, so all companies should consider the need to assess the implications of the new standard and develop implementation plans to address those implications. Of particular note, the new guidance may enable some companies to recognize revenue sooner than they typically do under existing accounting standards.

Further, companies with a longer delivery cycle, or those with nonstandard and complex contract terms, will be the most affected. These organizations will require greater resources from systems or processes to provide the necessary information to meet the data requirements to account for and describe revenue recognition.

The impact of the new standard could be far-reaching and potentially disruptive, as it may also affect processes and reporting associated with:

- Commissions, bonus and compensation structures
- Key financial performance metrics
- Partnerships, alliances and joint ventures
- M&A activities (working capital adjustments, revenue projections, post-deal multiple earnout provisions, etc.)
- Internal controls and SOX compliance
- Loan financial covenant compliance

While CFOs will likely own the responsibility to assess the requirements of the new standard, its implications and the appropriate transition plan, the responsibility for the design and implementation of solutions must be cross-functional in nature. The effort itself must be overseen through a project-driven discipline and approach (perhaps by a project management office (PMO) structure for large, complex organizations). Collaborative involvement and appropriate change management activities are critical to an effective and efficient revenue recognition transformation initiative. In particular, change management becomes a major determinant of success by overseeing the allocation of resources, establishing the transition framework and supporting appropriate training at all levels of the organization.

Many times, organizations are limited in terms of the internal expertise and resources they can re-deploy towards adopting a pervasive change successfully. Therefore, additional resources, including outside assistance, will likely be required to manage the initial transition requirements.

Some initial steps management teams should undertake include:

- Establish a consensus on the appropriate revenue recognition model and arrangements or classes of arrangements with customers.
- Assess the impact the new guidance will have on the accounting methodologies employed and systems deployed by management.

- Develop a plan to define the policy and supporting processes for each distinctive revenue stream.

We recommend a structured approach to reduce the risk of adoption while ensuring a sustainable revenue model. The approach should incorporate an understanding of the company's revenue model as well as the authoritative framework provided by the new standard. The sequentially-staged approach depicted below ensures that adoption of the standard leverages best practices during the different phases of implementation.



We believe the following components will prove to be critical success factors in defining and adopting the required changes:

- **Executive awareness and education** – Educate the senior management team, key stakeholders across the organization, the board of directors and the street on adoption alternatives under the new standard as well as the resulting potential impacts. Establish training materials and provide training to prepare the organization's personnel for the impact of the new standards.
- **Project management** – Manage the adoption process and provide for appropriate change management protocols.
- **Resourcing** – Identify and assess additional resource needs. Develop staffing plans for planning and execution.
- **Consider policy options** – Analyze current revenue policy and process against the proposed standard to identify expected changes. Consider the implications to upstream and downstream linked processes such as contract management and revenue assurance.
- **Gap analysis** – Perform a high-level analysis of system and data gaps:
 - Assess whether required information will be available from your existing processes.
 - Determine if system changes – or new data flows using the same systems – will be required.
 - Evaluate dependencies on external partner data and systems.
- **Transition strategy** – Develop a strategy for the transition methodology:
 - Select the transition method – either (1) retrospective application to each prior reporting period presented, or (2) cumulative effect reporting in the year of adoption. As discussed earlier, the difference between these two methods is primarily around restating comparative years.
 - Evaluate the challenges associated with retrospective adoption, e.g., registrants with the Securities and Exchange Commission (SEC) in the United States would be required to restate each year of the selected financial data presented in filings.
 - Consider whether to elect one or more of the practical expedients offered by the new standard for retrospective adoption.
 - Consider complexity of performing the transition and whether specific tools and systems may be required.

The revenue standard will apply to all uncompleted contracts (under current U.S. GAAP) as of the adoption date. The development of a transition and implementation plan will require careful analysis of the appropriate approach, including the selected reliefs to *retrospective* adoption.

The new standard requires specific disclosures that will enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. Specifically, it requires that an entity disclose qualitative and quantitative information about all of the following:

- Its contracts with customers (including a reconciliation of contract balances).
- The significant judgments, and changes in judgments, made in applying the proposed guidance to those contracts.
- Any assets recognized from the costs to obtain or fulfill a contract with a customer.

In addition, the standard amends the FASB's Topic 270 on interim reporting and IAS 34, *Interim Financial Reporting*, to require certain information to be disclosed for interim reporting periods. A nonpublic entity may elect not to provide some of the proposed disclosures (for example, a reconciliation of contract balances).

A Joint Transition

Concurrent with the release of the final standard, the FASB and IASB announced the formation of a joint Transition Resource Group (TRG). Comprised of preparers, auditors, investors and some regulators, the objective of the TRG is to facilitate a smooth transition. This approach is not new. When the fair value standard was issued (Topic 820, Fair Value Measurements and Disclosures, formerly SFAS 157), the FASB did the same thing to obtain information for its board and staff on implementation issues.

TRG meetings will be open to the public via webcast. While the TRG will not be issuing guidance, it will provide a forum for raising implementation issues and will discuss with the individuals raising the issues whether the new standard provides sufficient guidance and, if not, the diversity in practice that might develop and the diversity that is appropriate in practice or should be addressed in the standard-setting process. The FASB and IASB boards will convene afterward to decide if additional standard-setting is necessary.

What impact the TRG will have remains to be seen. Hopefully, it will serve as a catalyst for adding needed clarity during the transition process.

Summary

The FASB views this new standard as a reduction in complexity. However, U.S. GAAP and IFRS convergence raises numerous questions for companies as they transition to the new rules. Management should invest time now to assess the impact of these changes on the organization to identify and prioritize accounting, reporting and other infrastructure issues that require attention. The appropriate organizational personnel need to immerse themselves into the new standard and get educated as to its impact on top-line reporting and disclosure. Whatever the impact, there will likely be development and/or modification of policies and procedures, redesign of accounting and reporting processes, IT and ERP system controls updates or improvements, and program, project and change management issues, among other areas. For public companies, the choice is clear: Get started with planning and implementing the transition sooner than later – and stay tuned for commentary by the SEC staff as they provide guidance on how they expect issuers to adopt the new standard.

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