

New Year, New Revenue Recognition Considerations



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When do you recognize revenue from contracts with customers? What was once an easy question to answer is now one that will soon require a multi-step analysis. For private entities, Accounting Standards Update (ASU) 2014-09 will be required for annual reporting periods beginning after December 15, 2018. Although we are one full year from implementation, there is various information that needs to be gathered and organized in order to implement ASU 2014-09 correctly.

The core principle behind ASU 2014-09 is that “an entity should recognize revenue to depict the transfer of 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.” Simply stated, entities must recognize revenue as performance obligations are satisfied. In order to identify such performance obligations, the following process should be followed:

First, **contracts with customers must be identified**. Applicable contracts under the new standards are those that have approval of both parties, have commercial substance, and have probable collectability of substantially all the consideration to which the entity is entitled. In addition, the contract must have approval of both parties, along with corresponding payment terms. Once applicable contracts are determined, **performance obligations need to be identified therein**.

A performance obligation is a promise within a contract to transfer a good or service to a customer. This good or service should be distinct, meaning it is readily identifiable from other goods or services outlined in the contract. Contracts may have one or more performance obligations. The **corresponding transaction price of the contract must then be determined**.

The transaction price is the amount of consideration the entity expects to receive in return for the transfer of goods or services to the customer. This transaction price should take into consideration payables to the customer, existing financing components, non-cash, and variable considerations. Keep in mind the terms of the contract, as well as your standard business practices in determining the transaction cost. Once the transaction cost is determined, it can then be **allocated to the performance obligations** previously identified.

Each performance obligation is allocated a portion of the transaction price based on the standalone selling price of the goods or services being transferred. If a standalone selling price is not easily identifiable, then one should be estimated. One item to note is that reallocation of the transaction price based upon a change in standalone selling price is not permitted under this new standard. Now that each performance obligation is assigned a transaction price, **revenue can be recognized accordingly as the obligation is satisfied**.

As the implementation date for ASU 2014-09 draws near, it is imperative that data and information for all contracts with customers be gathered and analyzed based upon this five-step process. For further guidance, please reach out to your external CPA and [AICPA's Financial Reporting Center](#) (FRC). The FRC includes a list of conferences, webcasts, and other publications to keep you updated on the most recent developments regarding the standard's implementation.