



Our webinar will begin shortly



*Updates to the Revenue Recognition
& Lease Accounting Standards*

May 24, 2018

*Melissa Lacy
Seth Rensberger
Clark Schaefer Consulting*





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Questions

How to ask a question during today's webinar?

- Use the “Chat” or “Question” feature on the GoToWebinar panel.
- You can also email Sara O'Banion at sobanion@clarkschaefer.com.
- Questions will be addressed at the end of the webinar.

Interested in CPE for today's event?

CPE Option 1 (Digital method)

- Be logged into the webinar for at least 50 min.
- Complete three of our interactive polls
- Complete the webinar survey

CPE Option 2 (Paper method)

- Be logged into the webinar for at least 50 min.
- Record the three CPE codes on the CPE form (located in the Handout List)
- Complete the webinar survey
- Send completed CPE form to nboudreau@clarkschaefer.com

Today's Presenters



Seth Rensberger

Director, Cincinnati Office



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Today's Agenda

- Update on ASC 606 -
the Revenue
Recognition Standard
- Update on ASC 842 -
Accounting for Leases



Revenue Recognition

Why the change?



Why did we need a new standard?

Prior to Accounting Standards Update 2014-09:

GAAP \neq IFRS

Generally Accepted Accounting Principles *International Financial Reporting Standards*

As a result...



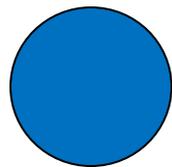
International
Accounting Standards
Board®

FASB FINANCIAL
ACCOUNTING
STANDARDS BOARD

...initiated a project to clarify the principles for recognizing revenue under GAAP

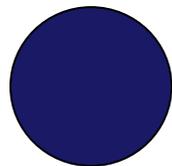
Know when it takes place...

- When exactly does it take place?



Public entity:

- *Effective for fiscal years no later than January 1, 2018*



Nonpublic entities:

- *Effective for fiscal years no later than the year ended December 31, 2019*
- *Could have adopted at the same time as public entities*

Expected objectives...

- Removes inconsistencies
- A more robust framework for addressing revenue issues
- Improves comparability of revenue recognition practices
- Useful information to users of financial statements
- Simplifies the preparation of financial statements

Revenue Recognition – ASC 606

Five Steps to the Core Principle



*Identify the
Contract*

*Identify
Performance
Obligations*

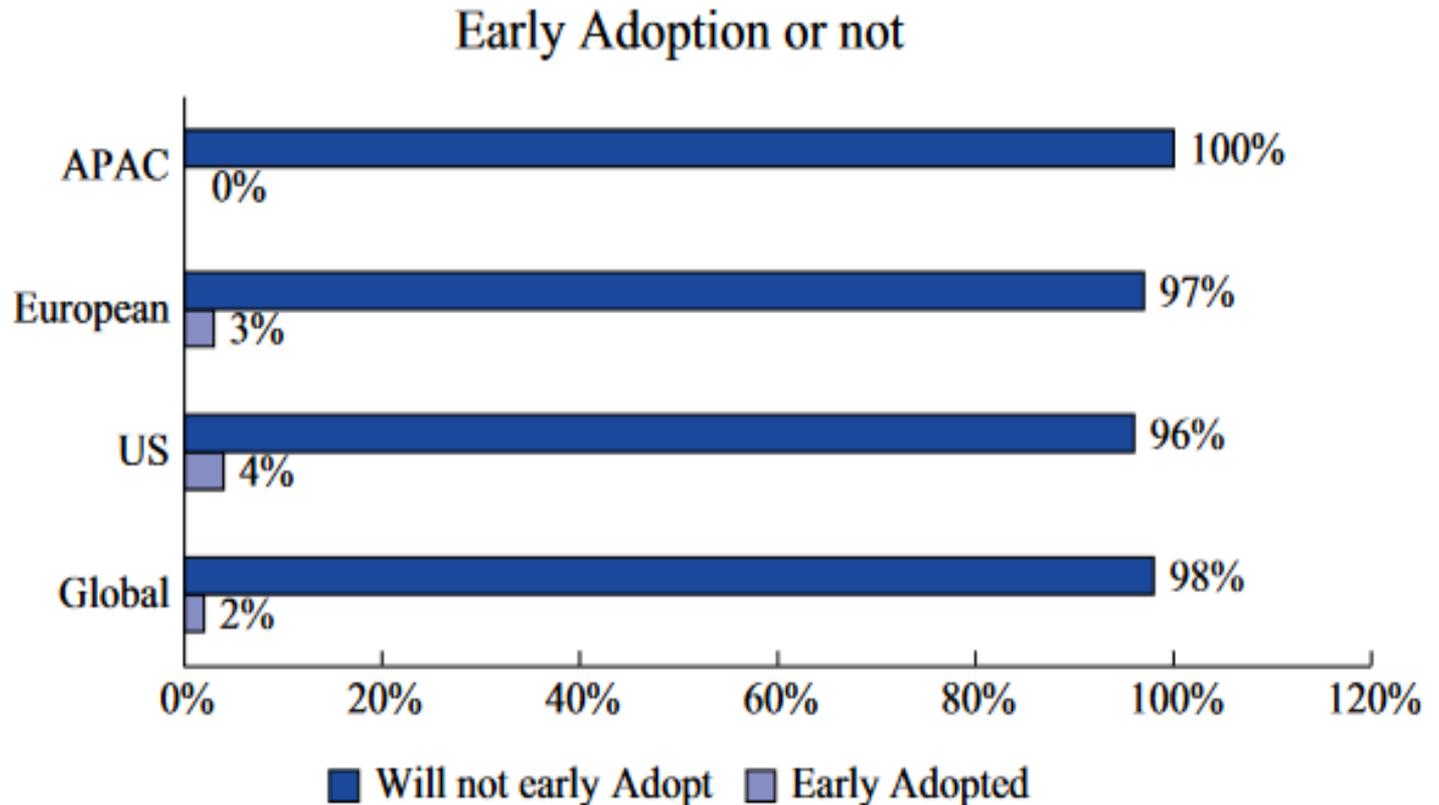
*Determine
Transaction
Price*

*Allocate
Transaction
Price*

*Recognize
Revenue*

Revenue Recognition – ASC 606

Survey of Early Adopters



Revenue Recognition – ASC 606



- Microsoft elected to adopt this standard using the full retrospective method.
- If the new approach had been applied for year ended 2016, Microsoft's revenue would have been \$6 billion (or 7% higher) than was stated.

Revenue Recognition – ASC 606

GENERAL DYNAMICS

- General Dynamics adopted Topic 606 on 1 January 2017.
- In its 2016 10-K, they provided restated revenue and operating earnings amounts that would have reduced revenue by \$792 million in 2016 and would have increased revenue by \$312 million in 2015.
- Operating earnings would have been reduced by \$575 million in 2016 and would have increased by \$114 million in 2015.

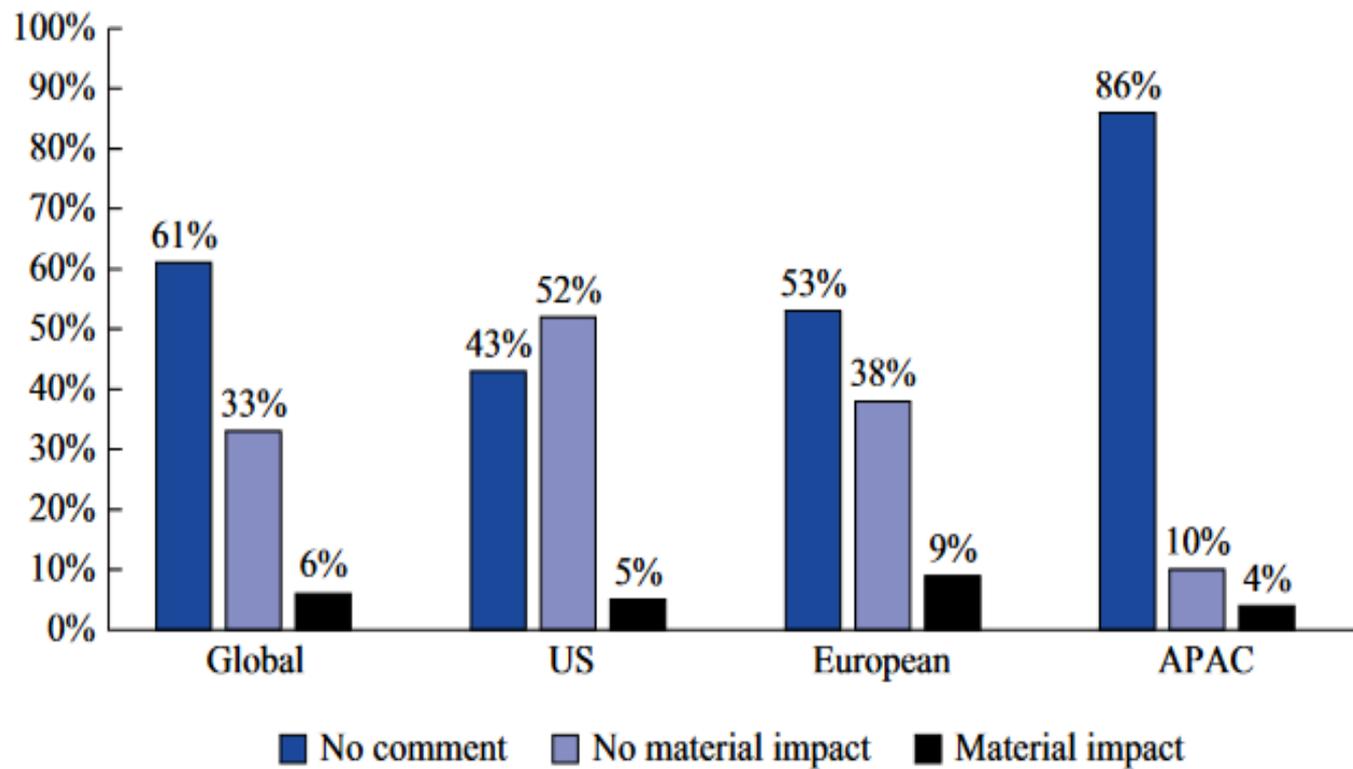
Revenue Recognition – ASC 606



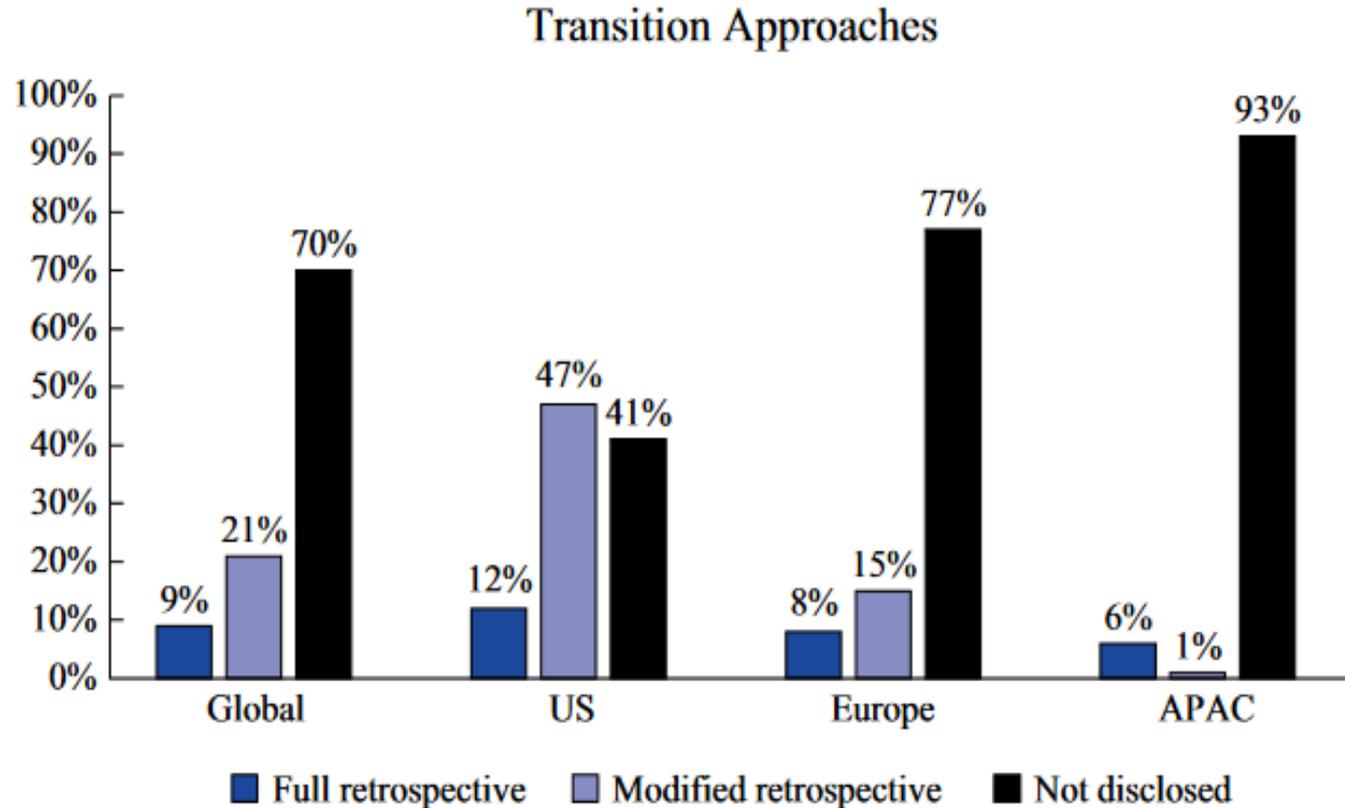
- Ford Motor Company adopted Topic 606 on 1 January 2017.
- In its 10-Q for the period ending 30 June 2017, Ford’s management stated the new revenue standard expected to be immaterial to net income.
- However, it resulted in \$736 million of higher revenue and \$1.44 billion lower “deferred revenue and other liabilities”.

Revenue Recognition – ASC 606

Expected Impact of Changes (300 Global Companies)



Revenue Recognition – ASC 606



Wrap up

For companies choosing the full retrospective method, a complete reworking of historical data is required for reporting, while the modified retrospective approach requires two sets of books to be maintained.

ASC 842 Overview

- Updated requirements adopted by FASB in February 2016 will fundamentally change how companies account for leases
- With implementation dates as early as December 2018, the new standards provide increased transparency around the financial obligations of lease agreements by requiring operating leases to be recognized on the balance sheet



ASC 842 Overview

The new standard requires several steps including:

- Identify all legal contracts
- Evaluate whether a contract contains a lease
- Apply the new standard to arrangements within the scope of ASC 842

ASC 842 Overview

With the (original) new standard, organizations were required to prepare *modified retrospective transition approach* to their financial reports beginning as early as January 2017.



ASC 842 Overview

ASC 842 originally required that entities separate lease components from non-lease components in a lease contract and treat each component separately.



Issues With Implementation

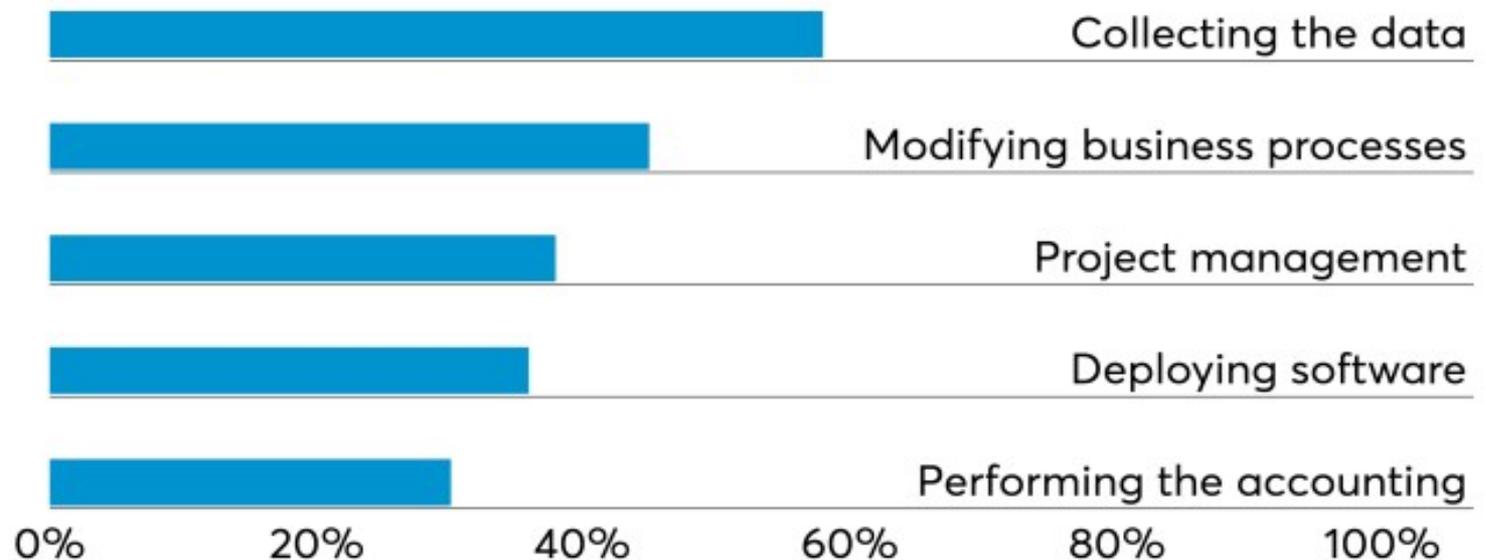
- Implementation more complex than expected
- Costs associated with the modified retrospective approach were excessive and slowing implementation

Issues With Implementation

What's the problem?

Companies share their biggest obstacles to implementation of the new lease accounting standard.

● Percent



Source: LeaseAccelerator

Issues With Implementation

Both lessors and lessees have requested transition relief and simplification to enable them to apply the new leasing guidance.



Proposed Amendments to ASC 842

The Board was sympathetic to this feedback, and so in November 2017 voted to propose amendments to the original standard.



Optional Transition Relief

The new standards include the following changes:

- Added an option for transition that would permit an organization to apply the transition provisions of the new standard at its adoption date instead of at the earliest comparative period presented in its financial statements.
- Add a practical expedient that would permit lessors to not separate non-lease components from the associated lease components if certain conditions are met.

Amendments to ASC 842

The new guidance allows entities the option to instead apply the provisions of the new leases guidance at the effective date (e.g., January 1, 2019), without adjusting the comparative periods presented.

Amendments to ASC 842

Therefore, an entity could elect to change its date of initial application to January 1, 2019. In doing so, the entity would:

- Apply ASC 840 in the comparative periods.
- Provide the disclosures required by ASC 840 for the comparative periods.
- Recognize the effects of applying ASC 842 as a cumulative-effect adjustment to retained earnings as of January 1, 2019.

Amendments to ASC 842

The entity would not:

- Restate 2017 and 2018 for the effects of applying ASC 842.
- Provide the disclosures required by ASC 842 for 2017 and 2018.

2017



2018



Amendments to ASC 842

The New Transition Method Will Affect Investors:

- The new transitions method takes away a substantial amount of insight into corporate leases.
- Investors won't be able to compare ASC 840 and ASC 842 reports side by side.
- Investors may remain in the dark about comparative information.



Amendments to ASC 842

Lessor's Separation of Lease and Non-lease Components

- Lessors often provide services to lessees in addition to the leased asset itself, such as maintenance services for the leased property or equipment.
- The new ASC 842 standard originally required lessors to separate lease and non-lease components
- ASC 842 would apply to the lease component, and ASC 606 apply to the non-lease component.



Amendments to ASC 842

However, the FASB received feedback from stakeholders indicating that the costs of complying with ASC 842's current separation and allocation requirements outweighed the benefits.

As a result, the FASB decided to amend ASC 842 to provide lessors with an optional practical expedient.

FASB's new lease standard allows them to forgo parsing out of the non-lease components of a contract from the value of the base rents lessees charge lessors.

Amendments to ASC 842

A lessor that elects the practical expedient will not be required to separate lease and non-lease components, provided that both of the following conditions are met:

- The patterns of revenue recognition for the components are the same.
- The combined, single unit of account would be classified as an operating lease.

Further, the lessor would be required to disclose (1) that it has elected the expedient and (2) the nature of the items that are being combined.

Amendments to ASC 842

Land Easements – New Amendments

- Now specifies that land easements – as rights to use land – are within the scope of the new leases standard and should be analyzed to determine if they meet the new definition of a lease.
- Grants an optional practical expedient that permits a company at transition to not assess whether expired or existing land easements are or contain leases that they had not previously accounted for as leases under current US GAAP.

Amendments to ASC 842

Wrap Up

- The revisions to the new standard do not change how the transition requirements are applied.
- They do not eliminate the substantial implementation burden that they will face under the new standards.
- Companies still have to design controls for all organizations that touch their leasing programs.

Amendments to ASC 842

FASB Chairman Russell Golden stated:

“The [updated] ASU is aimed at reducing unnecessary costs around implementation of the new leases standard without compromising the ultimate quality of information provided to investors.

It’s part of our ongoing effort to proactively address implementation issues raised by our stakeholders to ensure a successful transition to the new standard.”

Questions?



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Thank You



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