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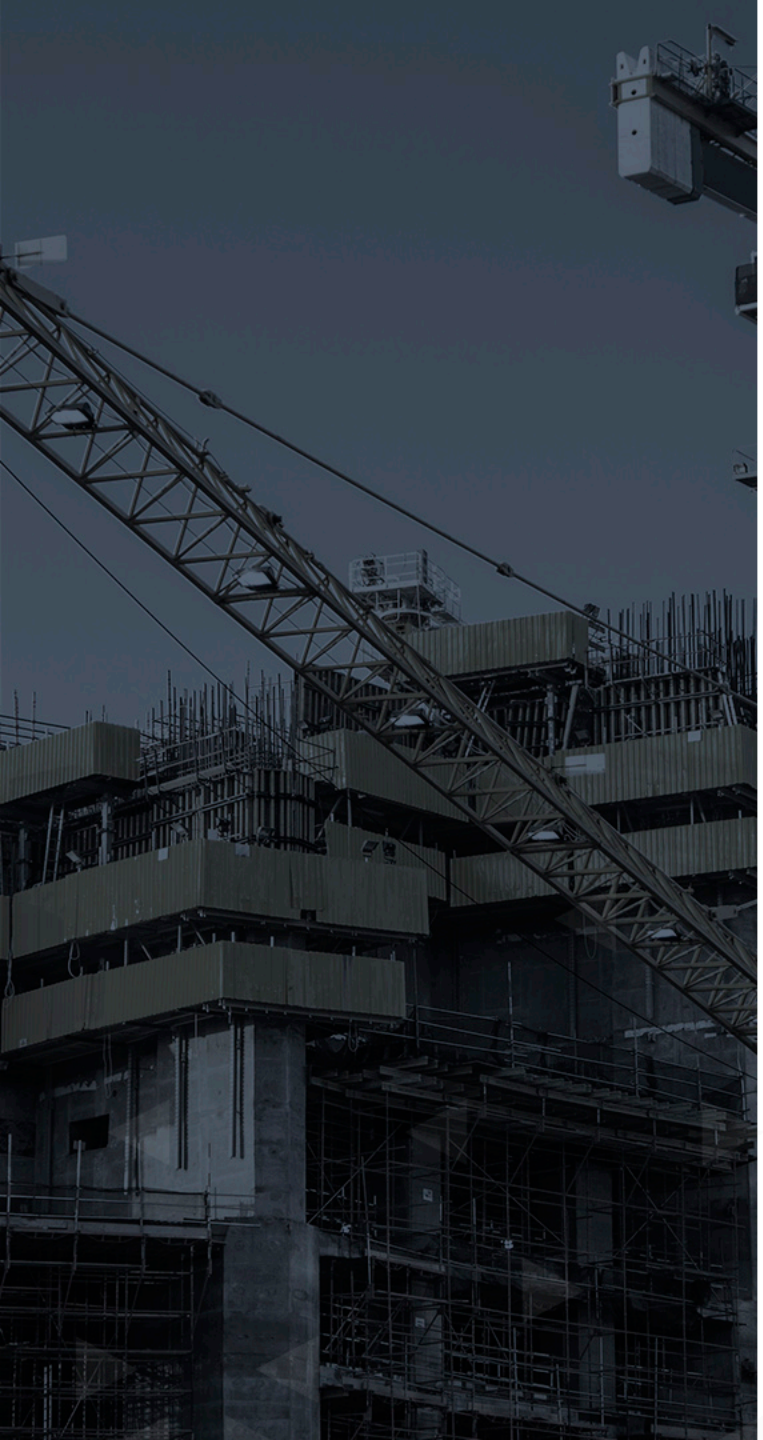

THOUGHTWARE®

Is Your Accounting House in Order?

Emerging Issues update

July 26, 2019

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Nickie Redick, CPA
Director

Nickie has more than thirteen years of experience providing audit, accounting and consulting services to a variety of clients, including manufacturing, distribution and construction companies and employee benefit plans. She also serves as the office industry team leader for construction and real estate.

She works with clients ranging in size from those with $10 million in revenue to large consolidated groups with revenues in excess of $1 billion, including clients with international operations. She has experience in audits for both private and public clients and in U.S. Securities and Exchange Commission compliance testing.

Nickie is a member of the American Institute of CPAs and Indiana CPA Society. She is a founding member of Executive Women in Finance in the Indianapolis area and serves as a member of the events committee. She also serves as treasurer for Hancock Hope House.

Nickie is a 2006 graduate of University of Indianapolis, Indiana, with a B.S. degree in accounting.

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Topics for Today

- New Accounting Standards
  - Revenue Recognition
  - Lease Standard
- Private Company Council
- Other Accounting Hot Topics

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New Accounting Standards – Revenue Recognition

Revenue Recognition

Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers*

- Effective for nonpublic companies for annual reporting periods beginning after December 15, 2018
  - Industry specific guidance replaced with a principles-based standard for all industries

Revenue Recognition – 5 Step Model

1) Identify Contract with Customer
2) *Identify Performance Obligations*
3) *Determine Transaction Price*
4) Allocate Transaction Price to Performance Obligations
5) Recognize Revenue When (or as) Performance Obligation Is Satisfied

AICPA Engineering & Construction Contractors Revenue Recognition Task Force Implementation Issues

1) Identifying the Unit of Account
2) Variable Consideration
3) Acceptable Measures of Progress
4) Uninstalled Materials
5) Impact of Termination for Convenience on Contract Duration
6) Contract Costs
7) Disclosures

Nonpublic Companies Implementation Modified Retrospective Approach

1) Review Year End 2018 Contracts in Progress Schedule
2) Identify Any Differences Between Current Treatments and Treatment Under ASU 2014-09
3) Any Differences Would be a Restatement to Year End 2018 Equity
4) No Differences – Still Need to Document Consideration

3 Key Impact Areas

- Identify Performance Obligations
- Variable Consideration
- Uninstalled Materials

Identify Performance Obligations

Revenue is to be recognized based on satisfying performance obligations on a contract-by-contract basis. Management will need to use judgment to determine if contracts include more than one distinct performance obligation or if one performance obligation is to be provided through multiple contracts.

Promised goods or services are considered distinct when they are:

- Capable of being distinct because the customer can benefit from the good or service on its own or with other readily available resources
- Distinct within the context of the contract – the good or service to the customer is separately identifiable from other promises in the contract

Variable Consideration

- Identify the transaction price including the probable amount of variable consideration
- Contract Amount on WIP Schedule = Original Contract +/- Change Orders +/- Variable Consideration
- Possible Variable Consideration
  - Performance Bonuses, Liquidated Damages, Claims, Unpriced Change Orders

Uninstalled Materials

When using cost-to-cost method to determine percentage of completion, only the costs incurred that contribute to the progress of satisfying the contract should be included in the calculation of gross profit to be recognized.

Costs of uninstalled materials could be treated as inventory until installation is complete. If treated as job costs, revenue should only be recognized equal to cost.

Uninstalled Materials

If ALL FOUR criteria below are met, cost incurred would not indicate the satisfaction of the contract and completion of the performance obligation:

1) The good is not distinct
   a) Readily useable in other construction projects without incurring significant cost to modify
   b) Inventoriable materials
2) The customer is expected to obtain control of the good significantly before receiving services related to the good
3) The cost of the transferred good is significant relative to the total expected costs to completely satisfy the performance obligation
4) The entity procures the good from a third party and is not significantly involved in designing and manufacturing the good

Revenue Recognition - Disclosures

- Disaggregation of revenue by major category
- Possible Categories
  - Type of good or service – Major product lines
  - Geographic region – Country, state or region
  - Type of contract – Fixed price or time and materials
  - Contract duration – Short-term or long-term contracts
  - Timing of revenue recognition – Point in time or over time

New Accounting Standards - Leases

Leases

Accounting Standards Update (ASU) 2016-02, *Leases*

- Effective for public companies periods beginning after December 15, 2018
- Effective for nonpublic companies for annual reporting periods beginning after December 15, 2019

Lease Classification

- Finance lease
  - Control is effectively transferred to the lessee
  - Similar currently to – capital leases
- Operating Leases
  - Control is not effectively transferred to the lessee
  - Similar currently to – operating leases

Balance Sheet

- Lease Liability
  - Present Value of Future Lease Payments

- Right of Use Asset
  - Lease Liability
  - Plus:
    - Initial Direct Costs
    - Lease Prepayments
  - Less:
    - Incentives Received

Income Statement

- Finance Lease
  - Lease Liability
    - Reduce using effective interest rate method
  - Right of use asset
    - Amortize on a straight line basis
  - Results
    - Interest Expense
    - Amortization Expense

- Operating Lease
  - Lease Liability
    - Reduce using effective interest rate method
  - Right of use asset
    - Amortize to achieve a straight line total lease expense
  - Result
    - Lease Expense

Important Key Points

- Consideration of all leases > than one year (election)
- Reasonably certain lease terms specifically in renewals
  - Contract based factors
  - Asset-based factors
  - Entity-specific factors
  - Market-based factors
- Embedded Leases in Long-Term Contracts

Private Company Standards

Private Company Standards

- ASU 2018-17 – Target Improvements to Related Party Guidance for Variable Interest Entities
  - Effective years beginning after 12/15/2020
  - Early Adoption is permitted

Other Accounting Hot Topics

Hot Topics

- Segregation of Duties
- Fraud Procedures
  - Hotline
  - Detective Procedures
- Big Data Projects
- Protecting Data

Questions?

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Thank You!

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