Understanding the New Revenue Recognition Standard: What Does it Mean for Auditors?

April 1, 2019

Session objectives

Fundamentals of the new revenue recognition accounting standard

Considerations for internal audit departments

Fundamentals of the new revenue recognition accounting standard

Objectives of the new revenue standard

Remove inconsistencies and weaknesses in existing requirements to improve comparability

Provide a more robust framework for addressing revenue issues

Provide more useful information through improved disclosure requirements

Simplify the preparation of financial statements by reducing the number of requirements by having one revenue framework

*IASB: International Accounting Standards Board/FASB: Financial Accounting Standards Board

Topic 606 requires careful consideration

"Revenue is one of the single most important measures used by investors in assessing a company's performance and prospects, regardless of a company's industry, the nature of its securities, or the capital markets it accesses. Revenue impacts key analytical ratios and bottom line earnings. **Companies cannot afford to get the accounting wrong – it deserves close attention by preparers, audit committees, and auditors.**"

Wesley Bricker, SEC Chief Accountant,

March 21, 2017

Introduction

FASB ASC Topic 606 replaced almost all existing revenue guidance, significantly increased the related disclosure requirements, and requires entities to use significant judgment and make new estimates. Entities will need to establish appropriate processes, systems, and internal controls to account for contracts with their customers under the new standard, which can include the following:

— Management will need to **update key accounting policies and business processes** as a result of adopting Topic 606.

— In adopting Topic 606, entities may have **gaps in both their accounting and data sources** that will need to be addressed.

— Entities will need to **add new controls or update current ones** based on these changes under Topic 606.

— Entities will also need to **gather information that has not historically been required for financial reporting purposes** (e.g., costs incurred in obtaining a customer contract or when performance obligations are expected to be satisfied).

— The level of **management judgment exercised, accounting estimates and disclosures** will also increase.

— **ASC 606 also increases the level of detail and disaggregation required in financial statement disclosures**, key controls around ensuring appropriateness, completeness and accuracy of disclosures should also be considered.

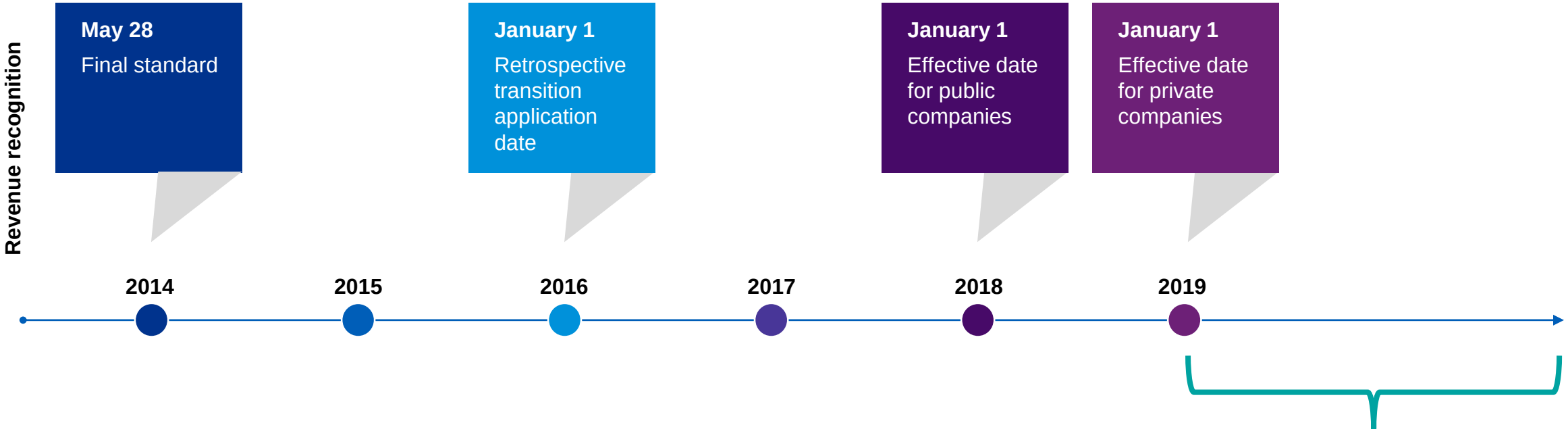
Objectives of the new revenue recognition standard

Simplify the preparation of financial statements by reducing the number of requirements by having one robust revenue framework for addressing revenue issues

Remove inconsistencies and weaknesses in existing requirements to improve comparability

Provide more useful information through improved disclosure requirements

Timing of the new standard



Internal audits to evaluate the effectiveness of new processes and procedures related to ASC 606

Scope of the new revenue standard

Contract

Standard does not apply to

- Lease contracts
- Contracts within the scope of ASC Topic 944
- Financial instruments and other contractual rights or obligations (e.g., receivables, debt and equity securities, liabilities, debt, derivatives, transfers and servicing, etc.)
- Guarantees (other than product or service warranties)
- Non-monetary exchanges between entities in same line of business to facilitate sales to customers

The core principle and the five-step model

Core principle

An entity recognizes revenue to depict 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

1. Identify the contract(s) with a customer
2. Identify the performance obligations in the contract
3. Determine the transaction price
4. Allocate the transaction price to the performance obligations in the contract
5. Recognize revenue when (or as) the entity satisfies a performance obligation

Step 1: Does a contract exist?

A contract is an agreement between two or more parties that creates enforceable rights and obligations. Enforceability is a matter of law. Contracts can be written, oral, or implied by an entity's customary business practices. Additionally:

…collection of consideration is probable*

…rights to goods or services and payment terms can be identified

A contract exists if…

…it has commercial substance

…it is approved and the parties are committed to their obligations

* The threshold differs under IFRS and U.S. GAAP due to different meanings of the term 'probable'.

Step 2: What are the performance obligations?

At contract inception, an entity shall assess the goods or services promised in a contract with a customer and shall identify as a performance obligation each promise to transfer to the customer either:

— A good or service (or a bundle of goods or services) that is distinct

— A series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.

Are promised goods or services distinct from other goods and services in the contract?

Capable of Being Distinct **AND** Distinct Within the Context of Contract (Separately Identifiable)

Yes → Performance obligation (PO)

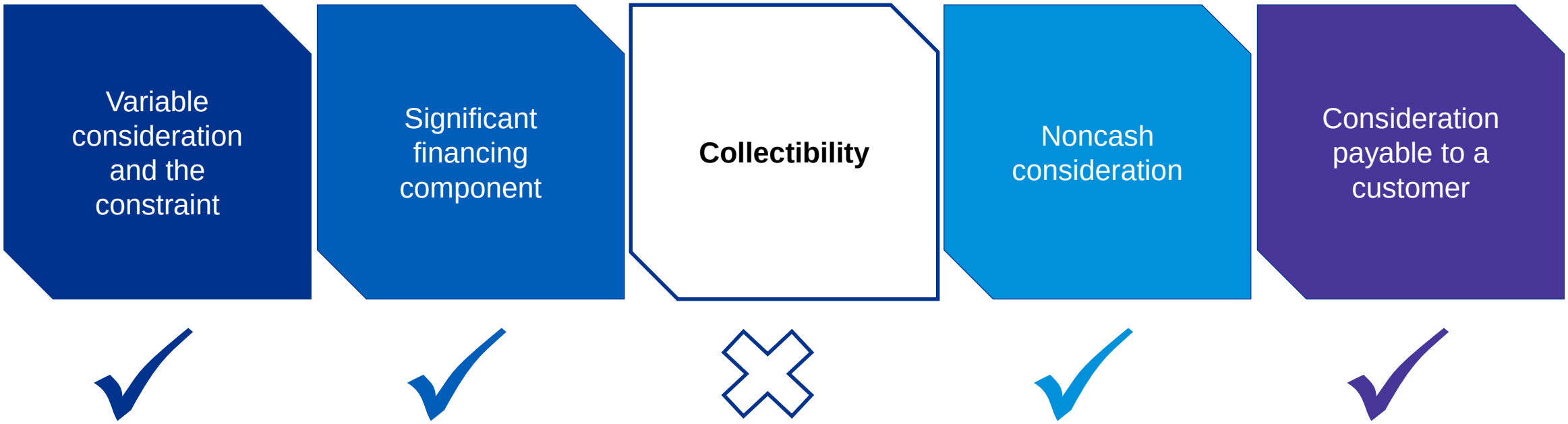
No → Not distinct – combine with other goods and services

Series of distinct goods or services are **substantially the same** + Each distinct good or service in the series is a **performance obligation satisfied over time** + **Same pattern of transfer** for each distinct good or service in the series = **A single performance obligation**

*The series guidance is **NOT optional**. If the criteria are met, the goods or services must be treated as a single performance obligation.*

Step 3: Determine the transaction price

***Transaction price* =** The amount of consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer (excluding amounts collected on behalf of third parties)



Step 4: Allocate the transaction price to the POs

Allocate based on relative stand-alone selling prices

Performance obligation 1	Performance obligation 2	Performance obligation 3

Determine stand-alone selling prices

Best evidence

Observable price

Fair value measurement

If not available

Estimate price

Adjusted market assessment approach

Expected cost plus a margin approach

Residual approach
only if selling price is highly variable or uncertain

Step 5: Recognize revenue

A performance obligation is satisfied over time if any of the following:

1. Customer simultaneously receives and consumes the benefits as the entity performs.

   Routine or recurring services

2. The customer controls the asset as the entity creates or enhances it.

   Asset built on customer's site

3. The entity's performance does not create an asset for which the entity has an alternative use and there is a right to payment for performance to date.

   Asset built to order

Exception for distinct licences of intellectual property

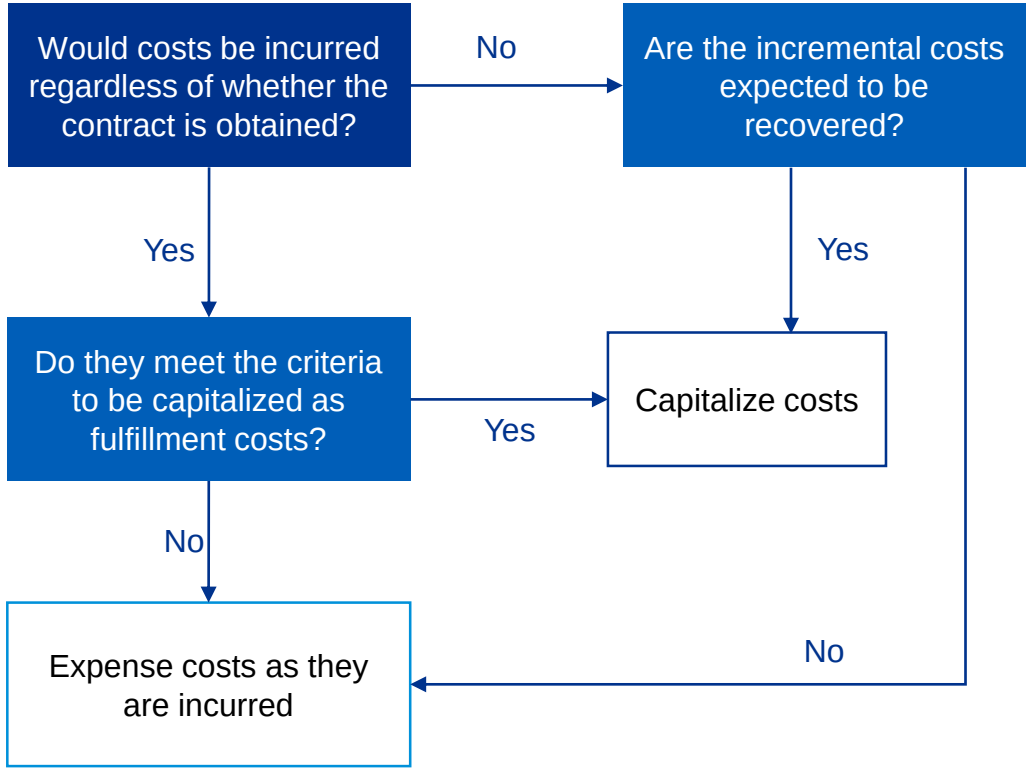
Point in time indicators:

Indicators that control has passed include a customer having…

- …a present obligation to pay
- …physical possession
- …legal title
- …risks and rewards of ownership
- …accepted the asset

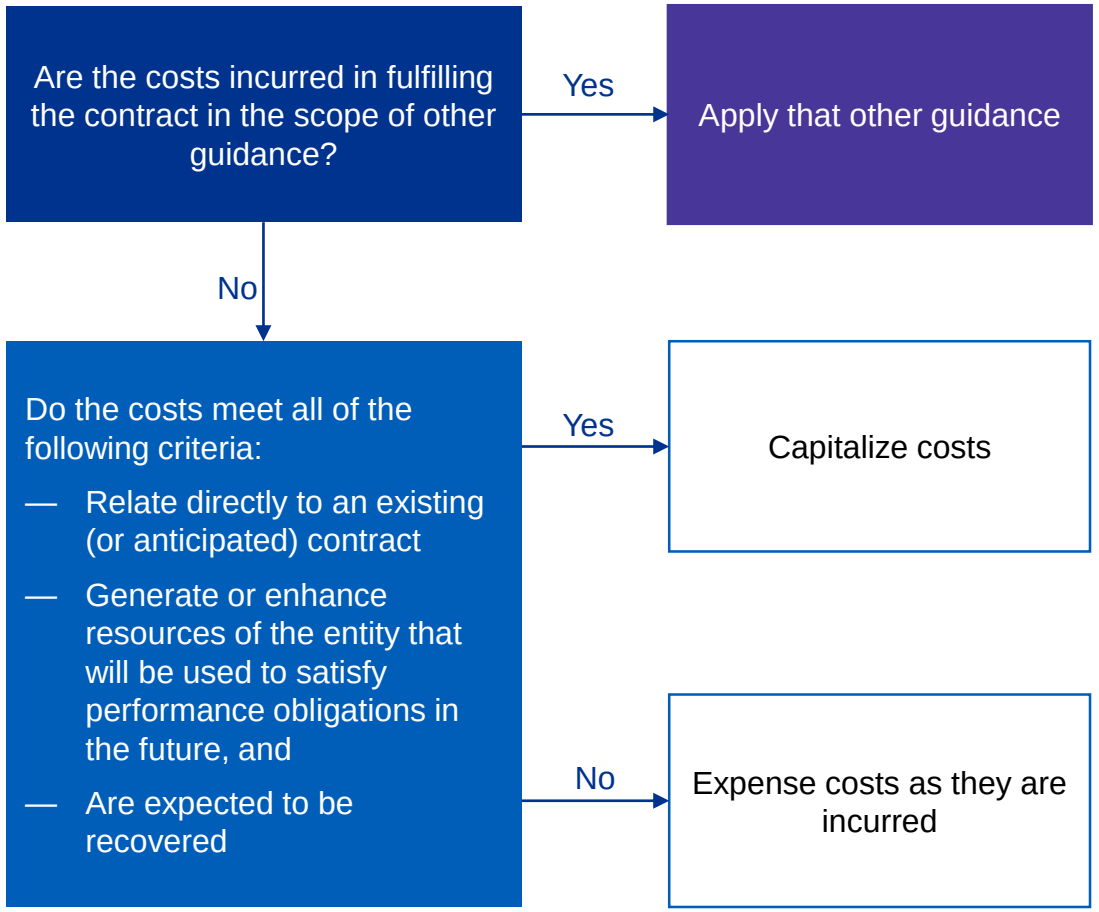
Accounting for costs:

Accounting for costs to obtain a contract:



As a practical expedient, capitalization of contract acquisition costs not required if the amortization period would be one year or less.

Accounting for costs to fulfill a contract:



Key accounts

The financial statement accounts and relevant assertions affected by Topic 606 may include the CEAVOP of:

- Revenue
- Contract assets
- Receivables
- Refund liabilities
- Taxes
- Inventory

- Contract liabilities
- Beginning retained earnings
- Capitalized costs to obtain a contract
- Capitalized costs to fulfil a contract

Presentation

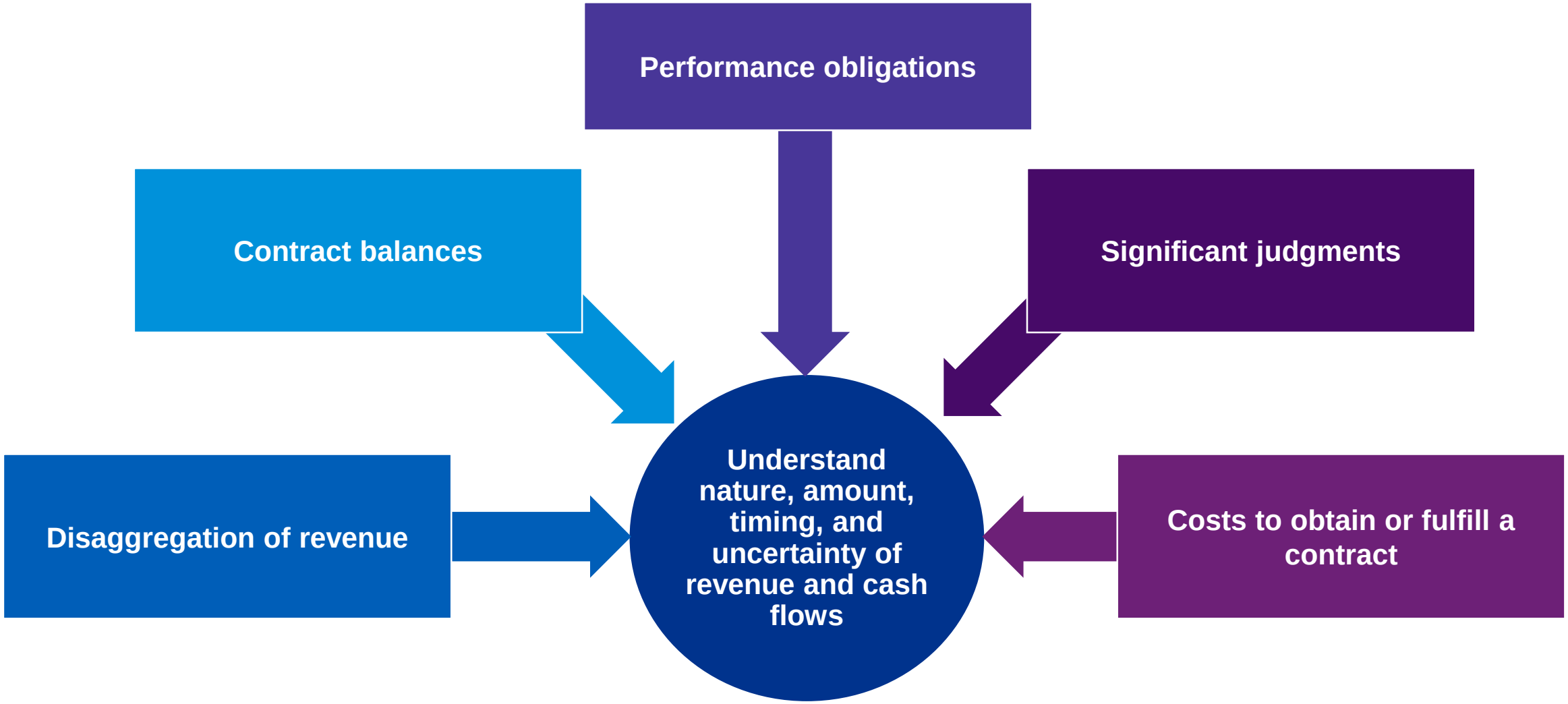
— A contract asset or contract liability is recognized when:
  - Entity performs by transferring goods or services
  - Customer performs by paying consideration to entity

— Unconditional right to consideration is presented as a receivable

— May use alternative descriptions for contract assets and liabilities; however, description must distinguish contract assets from receivables

— Contract costs capitalized are presented separately from contract assets

Disclosure requirements



Transition approaches

The following chart summarizes the transition options available to entities (based on a calendar fiscal year for U.S. public business entities):

Transition approach	2016/2017	2018	Date of cumulative effect adjustment
Retrospective	Restate for all contracts	Apply to all contracts	January 1, 2016
Retrospective Using One or More Practical Expedients (PEs)	Restate for all contracts except for contracts or estimates covered by the practical expedients elected by the entity	Apply to all contracts	January 1, 2016
Cumulative Effect at the Date of Adoption – elect to apply to all or only contracts not *completed*	No contracts restated; reported on the basis of legacy guidance	Apply to all contracts	January 1, 2018

Considerations for internal audit departments

A fresh look at internal controls and processes

"… as you evaluate your contracts with customers, it would be appropriate to take a ***fresh look*** not only at your historical accounting policies and how they may need to change but also at the ***design of the related controls*** (both existing and new) to ensure they are designed to operate in a manner that is sufficiently sensitive or precise to prevent or detect a material misstatement in the financial statements."

"… while implementation of the new revenue standard will obviously require taking a fresh look at business process-level controls, it is also ***important to keep in mind the other four components of internal control over financial reporting***, including control environment and risk assessment."

James V. Schnurr, SEC Chief Accountant,

March 22, 2016

Broad impacts on your organization?

For many companies, implementation of the new revenue recognition standard was not just an accounting exercise, as many different groups across the organization were impacted. These areas represent potential internal audit scope areas.

Accounting and Reporting Impact

- Impact of new standard and mapping to new accounting rules
- New accounting policies – historical results and transition
- Reporting differences and disclosures
- Tax reporting/planning

Financial and Operational Process Changes

- Moderate to significant financial statement changes
- Budget and management reporting
- Communication with financial markets
- Covenant compliance
- Opportunity to rethink business practices
- Coordination with other strategic initiatives

Systems and Process Impacts (including ERP upgrades)

- Automation and customization of ERP environment
- Impact on ERP systems, process documentation and SOX 404
- Expanded data needs may necessitate forecasting and other systems
- General ledger, sub-ledgers and reporting packages

Governance and Change

- Governance organization and changes
- Impact on internal resources
- Project management
- Training
- Multi-national locations
- Legal, Real Estate, Treasury, Contract Management, Forecasting, etc.

Internal audit considerations

Changes based on the new standard

- More extensive disclosures, including data that may not typically reside in Accounting
- New or modified processes, procedures and controls
- New judgments and incorporating additional qualitative information

SAPA 15 discussion areas

- Considering internal control over financial reporting (information system and manual controls)
- Identifying and assessing fraud risks
- Evaluating whether revenue is recognized in conformity with the applicable financial reporting framework
- Evaluating whether the financial statements included the required disclosures regarding revenue

Risk assessment → **Understand the flow of transactions** → **Identify the WCGWs** → **Identify controls** → **Evaluate design and implementation** → **Perform test of operating effectiveness** → **Perform substantive procedures**

COSO 2013 Framework Considerations

Control Environment

— Management needs to determine whether the entity maintained, in all material respects, effective ICOFR as of a specified date, based on the criteria established by a suitable framework. Nearly all U.S. registrants use the Internal Control – Integrated Framework published by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission as the framework.

— The **Control Environment** has a pervasive effect on an entity's system of internal control and therefore, **forms the foundation of effective ICOFR.**

— The COSO 2013 Framework describes the Control Environment, as:

- A set of **standards, processes, and structures** that provide the basis for carrying out ICOFR;
- The tone at the top (i.e., the tone set by the board of directors and senior management) with respect to ICOFR, including the integrity and ethical values of the organization; and
- Management's reinforcement of the tone at the top throughout the rest of the organization.

— **Management's tone** related to Topic 606 is a **key factor in an entity's successful implementation** of Topic 606.

— Entities will need to set an appropriate tone for adopting Topic 606 and **ensure individuals** are educated about its guidance to properly report financial amounts. Entities without these Control Environment aspects in place may have internal control deficiencies.

COSO 2013 Framework Considerations

Control Environment

Principles of the Control Environment	Topic 606 Considerations
Principle 1: The organization demonstrates a commitment to integrity and ethical values.	Has the tone at the top related to implementing Topic 606 been demonstrated by leaders of the organization?
Principle 2: The board of directors demonstrates independence from management and exercises oversight of the development and performance of internal control.	Has the Audit Committee accepted oversight responsibility in relationship to the entity's adoption of Topic 606?
Principle 3: Management establishes, with board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives.	Are authorities and responsibilities related to Topic 606 assigned across the entity and at all levels, and are they appropriate and sufficiently well-defined to enable accountability over operating units and functional areas?
Principle 4: The organization demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives.	Has the entity implemented a process to ensure adequate staffing levels to implement Topic 606, including contingency and succession plans?
Principle 5: The organization holds individuals accountable for their internal control responsibilities in the pursuit of objectives.	Is there a performance measurement and reward plan aligned with adopting Topic 606?

Training will be required for both finance and non-finance personnel, including the board, Audit Committee, senior management, and investor relations under Topic 606. Principle 4, "Demonstrates commitment to competence," of the COSO 2013 Framework, discusses the ability to hire, advance and retain competent individuals to support the financial reporting objectives of an entity.

COSO 2013 Framework Considerations (cont.)

Risk Assessment

— After the flow of transactions has been documented, management should identify What Could Go Wrong ("WCGWs") in the process where a material misstatement could occur and develop controls to prevent and/or detect the WCGW from occurring.

Principles of the Risk Assessment Component	Topic 606 Considerations
Principle 6: The organization specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.	Has the entity reviewed and updated its understanding of Topic 606 and considered the impact of changes on ICOFR?*
Principle 7: The organization identifies risks to the achievement of its objectives across the entity and analyzes risks as a basis for determining how the risks should be managed.	Has the entity updated its risk assessment based on the changes taking place under Topic 606?
Principle 8: The organization considers the potential for fraud in assessing risks to the achievement of objectives.	Has the entity considered in its fraud risk assessment the factors that may affect or create new fraud risks due to implementing Topic 606?
Principle 9: The organization identifies and assesses changes that could significantly impact the system of internal control.	Has the entity considered the effect of changes in the organization that will occur as a result of adopting Topic 606?*

Principle 9 of the COSO 2013 Framework requires management to assess changes in the external environment. Adoption of Topic 606 is a good example of a change to the external environment. Compliance with Principle 9 requires having controls in place to early identify and communicate changes that may have a significant effect on financial reporting and assess the risks resulting from those changes. The COSO 2013 Framework refers to such controls as "early warning systems."

*These needed to be considered in years prior to the adoption of Topic 606.

COSO 2013 Framework Considerations (cont.)

Risk Assessment

Potential fraud risk factors under Topic 606:

Incentives / pressures	Opportunities	Attitudes / rationalizations
— Management may try to maintain current accounting policies to avoid change and related costs — Management compensation (e.g. bonuses or equity awards) may be impacted by the amount of revenue and income recognized (e.g. revenue or net income targets) and therefore affected by Topic 606. — Management concluded prior to any assessment work that there would not be any impact from the adoption of Topic 606	— Complexity and judgment in accounting and reporting under Topic 606 — Increased use of estimates in the accounting for revenue — Inadequate processes and controls over Topic 606 — The ability to recognize revenue twice for the same transaction (once under Topic 605 before transition and again under Topic 606 after transition), or to minimize the amount of revenue that disappears into the 'black hole' (transition adjustment) through the one-time cumulative-effect adjustment	— Management has a history of earnings management or inaccurate estimates — Management does not believe certain requirements of Topic 606 result in better accounting — Management rationalizes that they should not be penalized under incentive compensation arrangements because of the transition to Topic 606

COSO 2013 Framework Considerations (cont.)

Control Activities

— After identifying the relevant reporting risks, management should **evaluate whether it has controls in operation** (i.e., in use) that adequately address the entity's financial reporting risks.

— As new reporting risks and WCGWs will be identified under Topic 606, **new and/or updated controls will need to be designed and implemented** to address these risks.

— Entities should ensure they have spent enough time scrutinizing the changed processes to design and implement appropriate controls related to Topic 606 to address the new risks.

— Presented below are Topic 606 considerations related to the Control Activities component:

Principles of the Control Activities Component	Topic 606 Considerations
Principle 10: The organization selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.	Has the entity identified controls related to Topic 606 that mitigate new risks under the new standard to an acceptable level?
Principle 11: The organization selects and develops general control activities over technology to support the achievement of objectives.	Has the entity updated IT application controls and related general IT controls based on the changes needed under Topic 606 to support the achievement of objectives?
Principle 12: The organization deploys control activities through policies that establish what is expected and procedures that put policies into action.	Have control activities been deployed to address the WCGWs identified with all requirements related to Topic 606?

COSO 2013 Framework Considerations (cont.)

Information and Communication

— The COSO 2013 Framework points out that “information is necessary for the entity to carry out internal control responsibilities in support of achievement of its objectives. Communication occurs both internally and externally and provides the organization with the information needed to carry out day-to-day internal control activities. Communication enables personnel to understand internal control responsibilities and their importance to the achievement of objectives.”

— Topic 606 requires **more information and data about the entity’s activities** than under current guidance for management to be able to properly account for contracts with customers and to prepare the necessary disclosures.

— This will include **using internal and external information to make appropriate judgments and estimates** where necessary. The process by which information is gathered across the organization is fundamental to any effectively designed system of internal control. Gathering the necessary information to apply Topic 606 will require seamless communication across the various functions of the organization.

— **Functions outside of controllership may be involved in the execution of controls** (e.g., FP&A now making estimates for accounting purposes). These groups may not have been involved in the past and therefore may be particularly important.

— There may be **information from external parties** (e.g., distributors, resellers, subcontractors, etc.) that will affect the accounting of Topic 606. Therefore, entities will need appropriate controls around that information (e.g., accuracy, completeness, timeliness, etc.).

— **Historical information is required** regardless of the transition method selected. For example, costs to acquire a customer that were previously expensed may now be required to be capitalized under Topic 606. This may require an entity to go back a number of years to obtain information on these costs depending on how long the customer contract life might be.

— Because historical data may be needed to determine the accounting, entities will need to be mindful of **what data needs to be retained** to reliably restate financial statements at the time of the transition. In addition, the **information required for disclosures** should also be considered.

COSO 2013 Framework Considerations (cont.)

Information and Communication

Principles of the Information and Communication Component	Topic 606 Considerations
Principle 13: The organization obtains or generates and uses relevant, quality information to support the functioning of internal control.	Does the entity have policies and procedures in place to ensure consistency in securing data, retaining data, and converting data into information suitable for financial reporting under Topic 606?
Principle 14: The organization internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control.	Does the entity evaluate the information relevance and reliability that will be used for financial reporting under Topic 606?
Principle 15: The organization communicates with external parties regarding matters affecting the functioning of internal control.	Does the entity communicate the functioning of internal control regarding Topic 606 with external parties?

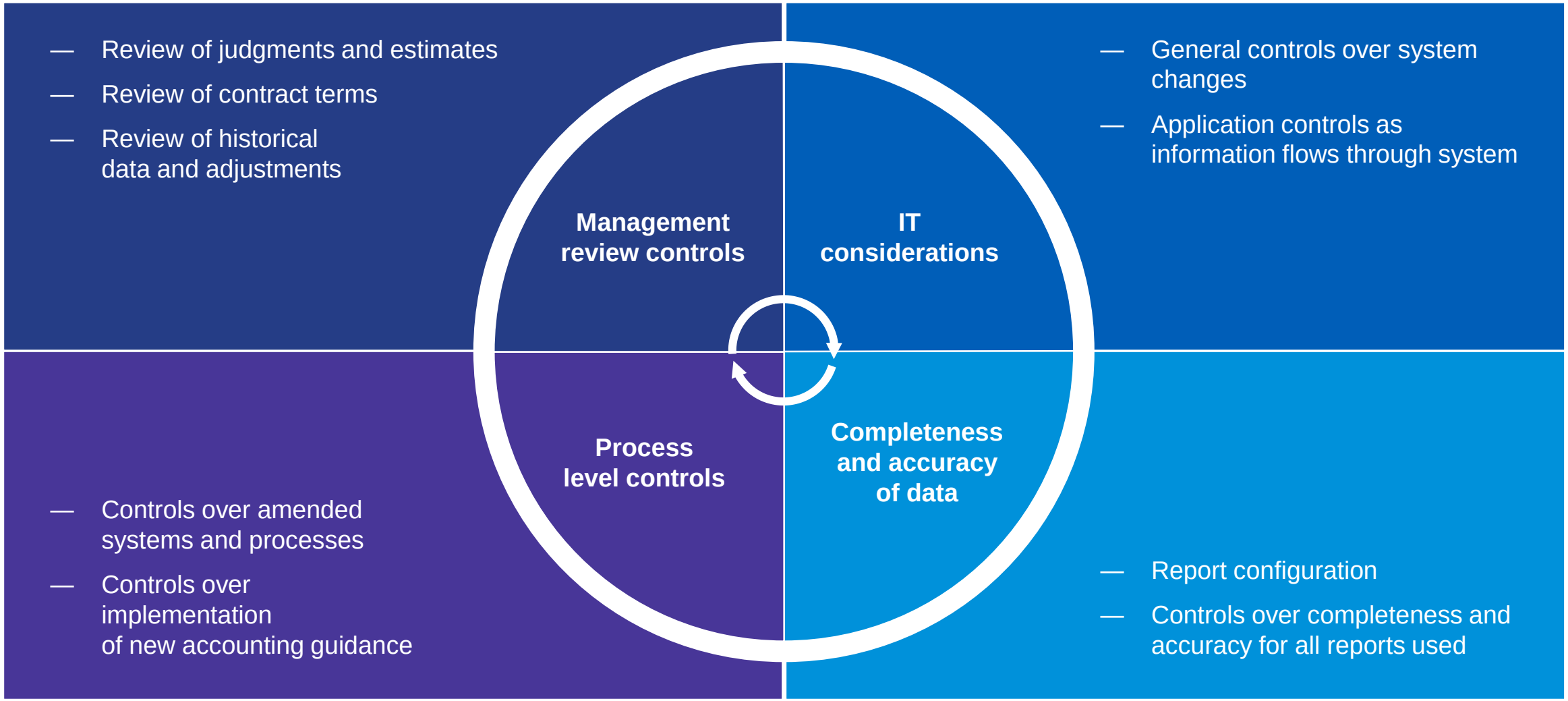
COSO 2013 Framework Considerations (cont.)

Monitoring

— Monitoring assesses whether the controls within each of the components of internal control are operating as intended. Results of effective monitoring also assist in determining required changes to the system of ICOFR to prevent or detect, on a timely basis, future errors in an entity's financial statements. Monitoring also includes evaluating the entity's overall compliance with the COSO 2013 Framework by evaluating the severity of identified deficiencies.

Principles of the Monitoring Component	Topic 606 Considerations
Principle 16: The organization selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.	Do the entity's monitoring activities consider a mix of ongoing and separate evaluations related to Topic 606?
Principle 17: The organization evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the board of directors, as appropriate.	Does the entity have policies and practices to evaluate the severity of the identified deficiencies related to Topic 606, including proper knowledge and training?

Revenue accounting



IT considerations

		Potential IT considerations
1	**Identify the contract(s) with a customer**	— System configuration of combining contracts based on date of contract and goods or services — System approval of a contract based on collectability criteria, taking into account price concessions
2	**Identify the performance obligations in the contract**	— System automatically separates out a good or service into separate performance obligations based on established criteria
3	**Determine the transaction price**	— Calculation of transaction price based on discounts, refunds or rebates — System calculation of interest income or expense when a significant financing component is involved
4	**Allocate the transaction price to the performance obligations in the contract**	— System calculation allocating discounts among performance obligations — System calculation allocating variable consideration among performance obligations
5	**Recognize revenue when (or as) the entity satisfies a performance obligation**	— Daily calculation of revenue recognized when the over time criteria is met — Calculation of revenue at a point in time by the system

Completeness and accuracy of data

		Information and data examples
1	**Identify the contract(s) with a customer**	— System reports of combined contracts — Spreadsheet of contract modifications — List of contracts within a portfolio
2	**Identify the performance obligations in the contract**	— Summary of options with material rights — List of distinct goods or services that constitute a single performance obligation
3	**Determine the transaction price**	— Report of contracts with a significant financing component — Summary of estimates of variable consideration and the method of estimation used — List of noncash considerations provided under contracts
4	**Allocate the transaction price to the performance obligations in the contract**	— Report of standard product stand-alone prices — Report of contracts where the residual approach was used to allocate the transaction price among performance obligations
5	**Recognize revenue when (or as) the entity satisfies a performance obligation**	— List of customers that have revenue recognized over time — Summary totals of input or output methods used to measure revenue over time — Report of shipping terms

Appendix

WCGW Considerations

Ongoing Control Considerations – Step 1 – Identify the Contract

A contract exists if…

- …collection of consideration is probable
- …rights to goods or services and payment terms can be identified
- …it has commercial substance
- …it is approved and the parties are committed to their obligations

Step 1 Concept	WCGW Considerations
— Contract with a customer — Legal enforceability — Termination clauses — Collectability concerns — Combining contracts — Contract modifications	— The entity applies the new standard to a contract that is not enforceable under laws and regulations in the jurisdiction of the contract, meaning the contract does not have enforceable rights and obligations. — The entity does not appropriately assess whether collection of contract consideration is probable due to inappropriate evaluation of the transaction price. — A legally enforceable contract with a customer that is oral or implied by the entity's customary business practices is not identified by the entity. — Consideration received is recognized as revenue for a contract that does not meet, or has not yet met, the contract existence criteria and the contract has not met one of the alternative recognition criteria.

Ongoing Control Considerations – Step 1 – Identify the Contract (cont.)

Key Control Considerations:

— Contracts are reviewed to determine whether they are in scope for ASC 606

— New contracts are reviewed under ASC 606 guidance to account for any potential revenue recognition implications (e.g., enforceability, collectability, inclusion of cash/non-cash considerations in determining transaction price, combination of two or more contracts, etc.)

— Changes to contracts are approved to ensure compliance with ASC 606. Impacts to recorded amounts are also assessed

— Contracts are reviewed for authorization and validity

Note: Many companies already had contract review control(s) in place, so consider whether existing controls were modified rather that implementing entirely new ones.

Ongoing Control Considerations – Step 2 – Identify Performance Obligations

Step 2 involves an entity identifying performance obligations to determine whether it promises to transfer either goods or services that are distinct, or a series of distinct goods or services that meet certain conditions. Key concepts and example WCGW considerations of Step 2 include:

Step 2 Concept	WCGW Considerations
— Capable of being distinct — Distinct in context of the contract — Series guidance	— The entity does not properly evaluate whether a customer can benefit from the good or service on its own or together with other readily available resources (capable of being distinct) when evaluating performance obligations, leading to the potential for inappropriate identification of performance obligations in a contract. — Promises or administrative tasks that do not transfer a good or service to the customer are inappropriately accounted for as performance obligations. — A series of distinct goods or services that are substantially the same are not combined into a single performance obligation when the series criteria in the new standard are met.

Key Control Considerations:

— Review the determination of performance obligations for completeness and appropriateness (i.e. obligations are appropriately included/excluded, and combined as needed). This control may be combined with a contractual review control as described in the prior step.

Ongoing Control Considerations – Step 3 – Transaction Price

The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer, excluding amounts collected on behalf of third parties – e.g., some sales taxes. In determining the transaction price, an entity considers:

Step 3 Concept	WCGW Considerations
— Variable consideration and constraint — Method of estimation — Consideration payable to a customer — Significant financing component — Noncash consideration	— Variable consideration (such as discounts, rebates, refunds, rights of return, credits, price concessions, incentives, performance bonuses, penalties, unexercised customer rights, or similar items) are not identified and/or otherwise considered in determining the transaction price. — The entity does not update its assessment of the constraint at the end of each reporting period, including consideration of new information or experience with contracts of a similar nature, resulting in inappropriate revenue recognition. — The entity does not identify a significant financing component in the contract that would require consideration in the transaction price, resulting in an inaccurate transaction price for the contract. — The entity does not measure as of the contract inception date noncash consideration received from a customer.

Ongoing Control Considerations – Step 3 – Transaction Price (cont.)

Key Control Considerations:

— Review of transaction price based on the terms of contract (including cash/non-cash/initial estimates of variable considerations)

— Initial estimates of variable consideration are reviewed, including method selected, estimated amount, assumptions, etc.

— Review of variable considerations during each reporting period, including review of assumptions, completeness and accuracy of input data used in calculations, appropriateness of model used, mathematical accuracy, etc. This includes updating/adjusting estimated amounts and reconsideration of constraints used.

— Review of financing components and verifying that interest expense is appropriately recorded/disclosed (as appropriate)

— Considerations paid to customers are identified, reviewed and appropriately classified.

Ongoing Control Considerations – Step 4 – Allocation Price

Step 4 involves allocating the transaction price to each performance obligation – or distinct good or service – to depict the amount of consideration to which an entity expects to be entitled in exchange for transferring the promised goods or services to the customer.

Step 4 Concept	WCGW Considerations
— Determination of stand-alone selling prices — Relative selling price allocation — Allocating variable consideration and/or discounts	— The transaction price is not properly allocated to each performance obligation in proportion to its stand-alone selling price. — The entity does not apply a consistent method to estimate the stand-alone selling price of other goods or services with similar characteristics. — The entity does not allocate a discount, if applicable, proportionately to all of the performance obligations in the contract. — The entity does not allocate variable consideration proportionately to all of the performance obligations in the contract.

Ongoing Control Considerations – Step 4 – Allocation Price (cont.)

Key Control Considerations:

— The allocation of transaction price to performance obligations is reviewed, including estimates of sales returns, the allocation of discounts, transaction price in excess of the sum of standalone selling prices, variable consideration, subsequent changes to the transaction price, nonrefundable upfront fees, etc.

— Review of standalone selling price (based on observable inputs), including assessing the appropriateness of those inputs in relation to the nature of the performance obligation(s) and financing components (if applicable).

— Review of standalone selling price (based on estimates), including includes assessing the method selected (adjusted market assessment, expected cost plus a margin, residual approach) and the estimated amount(s), including the completeness/accuracy of input data, the appropriateness of the model, the reasonableness of the assumptions, and the mathematical accuracy of the calculations.

Ongoing Control Considerations – Step 5 – Recognize Revenue

In Step 5, an entity recognizes revenue when or as it satisfies a performance obligation by transferring a good or service to a customer.

Step 5 Concept	WCGW Considerations
— Transfer of control — Recognizing revenue over time — Recognizing revenue at a point in time	— The entity, in determining whether the customer simultaneously receives and consumes the benefits provided by the entity's performance under the contract, does not appropriately assess whether another entity would need to substantially reperform the work that the entity had completed to date if the performance obligation were to hypothetically transfer. — The entity does not consistently apply the selected method of measuring the progress for each performance obligation throughout the contract with similar performance obligations in similar circumstances. — The entity does not sufficiently evaluate whether and when control has passed to the customer when recognizing revenue for performance obligations satisfied at a point in time, including consideration of the indicators that control has passed included in the new standard.

Ongoing Control Considerations – Step 5 – Recognize Revenue (cont.)

Key Control Considerations:

— Transfer of control and timing (point in time vs. over time) is reviewed to determine appropriate revenue recognition. A review includes identifying when control of a good / service is transferred to a customer based on terms of the contract, including consideration of criteria in ASC 606-10-25-27.

— Calculations of revenue recognized over time are prepared and reviewed. A review includes assessing the method selected (input or output method) and the estimated amount(s), including the completeness/accuracy of input data, the appropriateness of the model, the reasonableness of the assumptions, and the mathematical accuracy of the calculations.

— Estimates and/or revenue reversals to achieve appropriate cut-off under ASC 606/IFRS 15 are reviewed. A review includes assessing the model, data and assumptions used to determine the amount of revenue to reverse.

— Management reviews forecasts used to estimate progress toward satisfying a performance obligation. The estimation methods are assessed for reasonableness on a periodic basis, including assessing the GAAP applied, the model, data and assumptions used and the mathematical accuracy of the calculations.

Other Key Control Considerations

There are several other key control impacts which do not directly fall under one of the 5 criteria listed above:

Concept	WCGW Considerations
— Contract Costs — Licensing — Sales-or usage-based royalties — Sale with a right of return — Warranties — Principal versus agent	— The entity inappropriately capitalizes costs to obtain a contract when those costs would be incurred regardless of whether or not the contract is obtained. — The entity inappropriately capitalizes fulfilment costs that (i) do not relate directly to an existing contract or specified anticipated contract, (ii) do not generate or enhance resources of the entity that will be used to satisfy performance obligations in the future, or (iii) are not expected to be recovered. — The entity does not appropriately identify situations where a promise to transfer a good or service includes a license that establishes a customer's rights to the entity's IP, potentially resulting in inappropriate revenue recognition. — The entity does not update its measurement of the refund liability and asset at the end of each reporting period for changes in expectations about the amount of the refunds. — The entity does not account for a warranty as a separate performance obligation when the customer can purchase the good or service with or without the warranty.

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