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Non-Profit Notes Newsletter

Implementing the New Revenue Recognition Standard

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The Financial Accounting Standards Board (FASB) issued accounting standards update (ASU) 2014-09, Revenue from Contracts with Customers (Topic 606) in May 2014, almost five years ago. For not-for-profit organizations (NFPs), the wait to implement the ASU is finally over. NFPs must adopt changes required by the ASU for annual reporting periods beginning after December 15, 2018. In other words, organizations operating within calendar year ends should have already adopted the changes starting January 1, 2019. NFPs with June 30th fiscal year ends have until July 1, 2019 to implement the ASU.

Main Provisions

The FASB issued ASU 2014-09 with the intent to establish a clear set of criteria that an entity must meet or follow before recognizing revenue. The FASB worked in coordination with the International Accounting Standards Board (IASB) to converge previous guidance into one revenue recognition standard (ASC 606 and IFRS 15, respectively).

The core principle of the ASU is that an entity should recognize 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 exchanges for those goods and services.

To achieve the core principle, an entity should apply the following steps in the order presented:

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

Note that the ASU does not apply to contributions. It does, however, apply to program revenue, membership revenue, and other fees generated by NFPs. Grants and contributions fall under the scope of ASU 2018-08, Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made.

Steps Your Organization Should Take

Steps you should consider taking to implement the requirements under the ASU, as well as evaluating the effects of the changes on your organization, include:

- Take an accurate inventory of all contracts with customers and evaluate all revenue streams to identify potential revenue sources that may be affected by the ASU;
- Review terms of contracts for performance obligations that could impact the timing of revenue recognition;
- Review existing internal controls and processes that may need to change to address the requirements under the ASU;

- Review monthly cut-off and closing procedures to ensure proper reporting of revenue under the new standard;
- Consider the effect(s) on your financial statements using one of two options for adoption of the ASU (see below).

Adoption

In the initial year of application (i.e., calendar 2019), the ASU allows one of two options: (1) the full retrospective method, ***or*** (2) the modified retrospective method.

Under the *full retrospective* method, in the year of implementation, an NFP would apply changes to prior period financial statements as if the ASU was already in effect in the prior period. For example, when an organization prepares fully comparative financial statements for 2019 and 2018, it would apply the requirements of the ASU to 2019 as well as 2018.

Under the *modified retrospective* option, an NFP would apply the ASU retrospectively only to contracts that have not been completed as of the date of the initial application of the ASU (i.e., 2019), without having to adjust prior periods.

Financial statement disclosures under the modified retrospective option must include:

- The use of the modified retrospective method;
- The amount by which each financial statement line item is affected by the adoption in the year of application.

Contact Us

If your not-for-profit organization needs assistance with implementing the new revenue standard or with any other accounting, auditing, tax or business consulting services, please contact the partner in charge of your account or:

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