Maner Costerisan
Certified Public Accountants
Business & Technology Advisors

Maner Costerisan PC
2425 E. Grand River Ave.
Suite 1
Lansing, MI 48912-3291
T: 517 323 7500
F: 517 323 6346
www.manercpa.com

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We want to make you aware of a significant accounting change and the potential impact on your Company. Effective January 1, 2019, privately held companies will be required to change how they recognize revenue in their financial statements. We want to bring this change to your attention by briefly explaining the new accounting standard, note some areas specific to the telecommunications industry, and provide a list of items your company may need to consider in order to implement the new standard.

To provide assistance with the implementation and transition to the new revenue recognition standards, we will be offering the following webinars:

Telecom Revenue Recognition – Part 1	April 19, 2018	9:00-10:00am EST
Telecom Revenue Recognition – Part 2	April 24, 2018	9:00-10:00am EST

We will forward information on registering for the webinars at a later date.

In addition, we will be offering one-on-one training, implementation guidance, and implementation guides after the webinars.

New revenue standard

In 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers.* The new ASU will significantly change US Generally Accepted Accounting Principles (GAAP) and enhance comparability of revenue recognition practices across companies and industries.

Existing GAAP contains numerous standards regarding the recognition of revenue from customer contracts, including a variety of specialized standards applicable only to certain industries or transactions. This difference in applying the rules has led to different accounting for similar transactions by different industries. Additionally, the required disclosures of a company's accounting for revenue has been limited, providing very little information.

The ASU adopts a single process for all companies and transactions. Companies will also be required to have more detailed disclosures related to their contracts with customers. Under the new ASU, companies may end up reporting revenue on their financial statements earlier or later, which could influence investors' perceptions of the company's performance.

The new GAAP revenue rules are based on the core principle that companies should recognize revenue as the transfer of promised goods or services to customers in an amount that reflects the consideration (payment) that the company expects to receive or be entitled to, in exchange for the promised goods or services. The ASU specifies five steps a company should follow to determine when, and how, revenue from contracts with customers is to be properly recognized.

Step 1 - Identify the contract with a customer

The ASU only applies to contracts a company has with customers, and the contracts must meet certain criteria. All other revenues not meeting the criteria to be a considered a contract with a customer will continue to be recognized under the current revenue recognition rules. There may be some circumstances where a company will need to combine contracts and account for them as a single contract. The ASU does allow the "portfolio approach" to be used for similar contracts.

Step 2 - Identify the company's performance obligations (or promises) under the contract

The ASU defines a performance obligation as a distinct good or service, or a series of distinct goods or services that are substantially the same. A good or service qualifies as "distinct" if; a) the customer can benefit from the good or service on its own or together with other resources readily available to the customer, and b) the promise to transfer the good or service is identifiable from other promises in the contract. A company with contracts having multiple performance obligations may need to account for each performance obligation separately depending on the terms in the contracts.

Step 3 - Determine the transaction price

Under the ASU, the transaction price is defined as the amount a company expects to be entitled to in exchange for transferring promised goods or services to a customer. There are multiple factors that will need to be considered when determining the transaction price, including discounts, variable payments, financing, etc. The ASU also contains rules for how to account for contract modifications.

Step 4 - Allocate the transaction price to each performance obligations in the contract

The ASU guidance specifies allocating the transaction price according to the "standalone selling price" of each distinct good or service promised in the contract. Any discounts, or variable payments, should be allocated between all the performance obligations. A discount for bundled services should be allocated between all the distinct services in the bundled contract.

Step 5 – Recognize revenue when (or as) performance obligations are satisfied

Under the new ASU, revenue will be recognized when (or as) a company satisfies a performance obligation by transferring the promised good or service to a customer. In other words, when the customer obtains control of the good or service. If a performance obligation is satisfied over time, then revenue will be recognized over the same time period regardless of how and when the customer pays for the good or service.

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Disclosure requirements

Under existing GAAP, the required disclosures for revenue are limited and require only the description of a company's revenue-related accounting policies and the policies' effects on revenue, if significant. Investors and other users of financial statements reported they found the disclosure requirements for revenues to be insufficient.

The new ASU substantially expands disclosure requirements, requiring qualitative and quantitative disclosures to provide users of financial statements with useful information about the company's contracts with customers. Required disclosures will include information about the nature, amount, timing, and uncertainty of revenue that is recognized.

Likely effects on telecommunications industry

Many companies may be expected to record revenues earlier to account for the effects of variable consideration, such as sales incentives, discounts, and warranties. The change is expected to have an especially dramatic effect on certain industries. Providers that routinely sell goods or services in bundled packages or enter into contracts that include variable payment terms, or frequently sell a customer a device at the same time as a service plan could see accelerated recognition of revenue. Under the current standards, these companies recognized revenue only to the extent they actually received cash.

At this time, the Federal Communications Commission (FCC) has made no indications there will be a change on how regulated revenues are recorded under the new ASU. Companies may need to continue to record the regulated revenues based on FCC rules, and record the difference between what should be recognized as revenues under the new ASU and the FCC rules separately.

The ASU guidance for telecommunications excludes universal service and high cost loop support including CAF BLS, CAF ICC, ACAM, and HCLS from the requirements under the new standard. These revenues are not paid on behalf of a specific customer, and the FCC and USAC do not meet the definition of a contract with a customer. Therefore, these revenues will continue to be recorded under the current revenue standards.

Additionally, companies will need to review their contracts with affiliates. Revenues recognized under the new ASU on one company may not match the expense recorded on the affiliate company.

The ASU applies only to revenues from contracts with customers. Those contracts that will continue to be covered by other FASB rules include insurance contracts, leases, financial instruments, guarantees, and nonmonetary exchanges between entities in the same line of business to facilitate sales. Although, some leases, such as leases of dark fiber and transport, may actually be contracts with customers and not leases depending on what the customer is leasing (service or goods).

Treatment of costs related to obtaining or fulfilling customer contracts

The ASU includes rules for accounting for costs related to obtaining or fulfilling a contract with a customer. Some incremental costs of obtaining a contract could be recognized as an asset and be amortized over the life of the contract. These costs may include labor, materials, costs related directly to a contract, and costs explicitly charged to a customer under contract.

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Making the transition

It is important to start communicating with accounting, tax, cost consultants, etc. on how the new ASU standard will impact your company and to begin planning for new practices and internal controls to implement and apply the new standard. Other items to consider:

- Learn the new revenue recognition rules.
- Determine what contracts fall under the new standard by applying the 5-step model.
- Determine if a change in revenue recognition will impact debt covenants, revenue requirements, or other agreements.
- Consider if any business practices or contracts should be changed or modified.
- Begin drafting footnote disclosures to help identify information needing to be tracked to ensure the company has the data necessary to adopt and disclose the new revenue standards.

Conclusion

The new Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers* will significantly change how companies are recording and reporting their revenues from contracts with customers. The time involved to learn, plan, and implement the new standard will be significant, and the effective date of implementation for private companies is fast approaching.

Please contact our office if you would like further information.

Maner Costerisan PC

Jeffery A. Irwin, CPA
Principal
Direct line: (517) 886-9575
E-Mail: jirwin@manercpa.com

Christy Sommers, CPA
Senior Manager
Direct line: (517) 886-9576
E-mail: csommers@manercpa.com

Zack Skryzniarz, CPA
Senior Manager
Direct line: (517) 886-9565
E-mail: zskrzyniarz@manercpa.com

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