



Now is the Time to Prepare for New Accounting Standards

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It has been a busy few years for accounting industry regulators like the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB). They have issued two far-reaching new accounting standards that will become effective soon. This article will provide an overview of these new standards and how your company should be preparing for their implementation.

New Revenue Recognition Standard

Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*, was issued by the FASB and the IASB in May of 2014. This new standard represents an important change in U.S. generally accepted accounting principles (GAAP) that will affect the accounting practices of any business required to complete GAAP-compliant financial statements, as well as the way such companies conduct business via customer contracts.

Commonly referred to as the new Revenue Recognition Standard, ASU 2014-9 is a principles-based standard for recognizing and reporting revenue from long-term contracts. The FASB's and IASB's objective with the new standard was to create a more consistent reporting framework across all industries so that users of financial statements can make more accurate comparisons and evaluations. To this end, much of the detailed, industry-specific revenue guidance that companies have traditionally relied on was replaced by a set of broad objectives.

However, this created a lot of uncertainty, so the FASB decided last year to push back the original implementation deadlines. The new Revenue Recognition Standard will now go into effect as follows:

- **Publicly traded companies:** Effective starting the first annual reporting period beginning after December 15, 2017. Typically, this will be either calendar year 2018 or fiscal year 2019.
- **Privately held companies:** Effective starting the first annual reporting period beginning after December 15, 2018. Typically, this will be either calendar year 2019 or fiscal year 2020.

To help companies apply the new Revenue Recognition Standard, the American Institute of Certified Public Accountants (AICPA) has formed 16 different industry task forces that are responsible for developing an updated AICPA Accounting Guide on Revenue Recognition. The guide will include illustrative examples of how to apply the new standard.

In preparation for the effective dates noted above, you should begin evaluating your company's revenue streams to determine which ones (if any) result from service contracts. You can then determine whether revenue should be recognized at a single point in time or over a longer period of time. According to the new standard, you should follow a five-step process for recognizing revenue from such contracts:

1. Identify the contract 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.

New Lease Accounting Standard

Accounting Standards Update (ASU) No. 2016-02, *Leases (Topic 842)*, will fundamentally change lease accounting under GAAP. The new Lease Accounting Standard will require businesses that lease assets (including vehicles, real estate and equipment) for more than one year to report their lease obligations on the balance sheet. Currently, lease obligations are usually structured as off-balance-sheet transactions — this minimizes debt on the balance sheet, which tends to make it easier for companies to obtain financing.

Under ASU No. 2016-02, the present value of scheduled operating lease payments of more than one year must be reported as a liability on the balance sheet. This liability will be offset by reporting a “right-of-use” value of the asset. This way, the overall statement will remain in balance.

The biggest impact of this change for most companies will be the effect it could have on key financial ratios by adding more debt to the balance sheet. This could affect debt covenants with lenders and/or make it harder to obtain financing in the future. Therefore, you will want to talk to your lenders and investors well before the new standard takes effect to avoid any unpleasant surprises.

The new Lease Accounting Standard will take effect for publicly traded companies for interim and annual reporting periods beginning after December 15, 2018, and for privately held companies for interim and annual reporting periods beginning after December 15, 2019.

While the effective dates for the new Revenue Recognition Standard and the new Lease Accounting Standard are still a year or longer away, you should begin getting ready for them now. An outsourced CFO services provider can help you prepare for the potential impacts of these new accounting standards.

Concluding Thoughts

Two new accounting standards issued by the FASB and the IASB will become effective soon: the new Revenue Recognition Standard and the new Lease Accounting Standard. These could have a significant impact on your company’s accounting practices, so now is the time to begin preparing for them. An outsourced CFO services provider can help you determine the potential impact of the new accounting standards on your company and plan accordingly.

About CFO Edge

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