REVENUE RECOGNITION:
As Easy as Depreciating a Fixed Asset

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Contents

Next

ASC 606 COMPLIANCE REQUIREMENTS MADE EASY BY NETSUITE'S ADVANCED REVENUE MANAGEMENT AND SUITEBILLING

In December of 2017, the most significant changes to accounting standards handed down by the FASB (Financial Accounting Standards Board) in decades will take effect for public companies, with deadlines for private companies not far behind. Known as ASC 606, the regulations provide standards for revenue recognition.

As the deadlines quickly approach, many companies are still struggling to prepare. In a late 2016 survey conducted by PWC, more than 50 percent of the respondents indicated that they were less than 50 percent of the way toward implementing the new accounting standards. They also indicated that they considered disclosure requirements the most difficult aspect of the regulations to meet. Those surveyed also said that ASC 606 would tax IT systems and present significant changes to accounting policies and procedures.

What's more, the new regulations will have wide reaching effects that extend well past finance processes and personnel, and have the potential to affect operations, legal and even compensation packages tied to revenue.

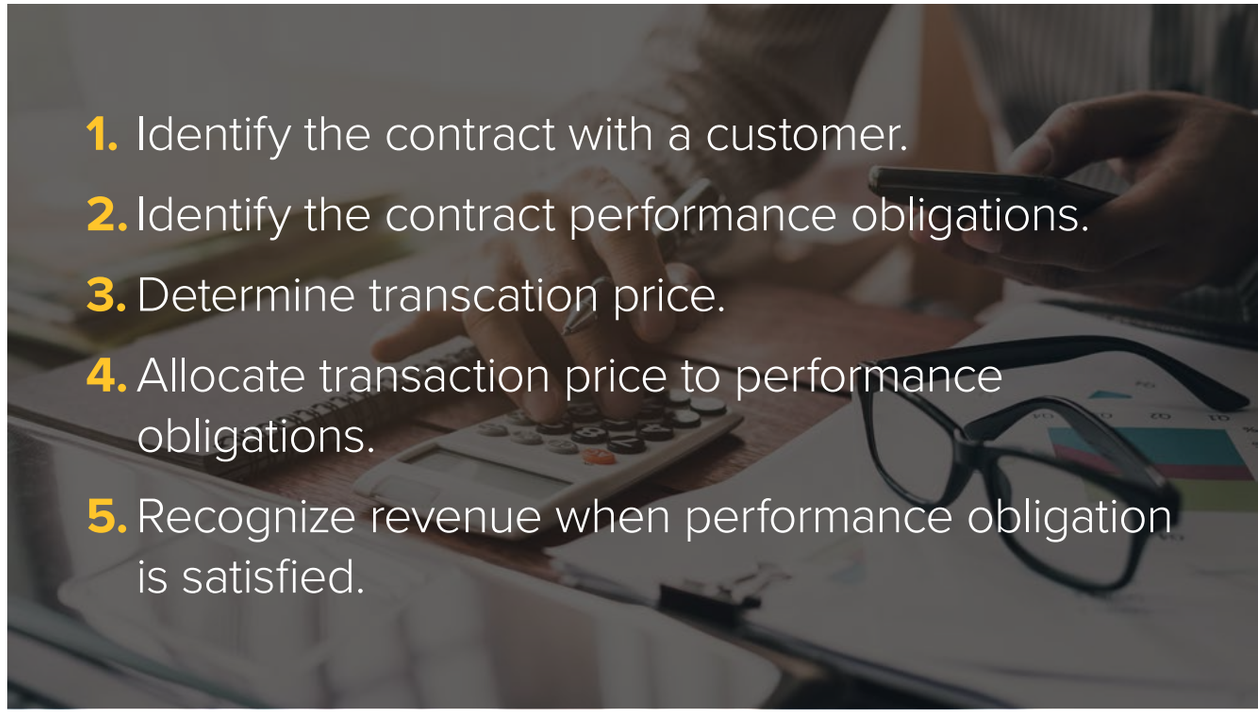
It's easy to become vexed by the new standards and overwhelmed at how to comply. But it can be quite simple—even as simple as depreciating a fixed asset. With the right software that manages seamless billing processes all the way through revenue recognition, businesses can ease compliance with ASC 606.

CHALLENGES IN ASC 606 COMPLIANCE

Adoption is required by Dec. 17, 2017 and Dec. 17, 2018 for public companies and private companies, respectively.

By then, revenue must be recognized on delivery of the performance obligations, defined in five steps.

Companies must identify the contract with the customer, identify the performance obligations in the contract, determine the transaction price for the contract, allocate the transaction price to the performance obligations and recognize revenue when or as the entity satisfies the performance obligation.



The Five Defined Steps of ASC 606

Even deciding how to implement compliance presents complexity for organizations. There are three adoption models: full retrospective, modified retrospective and cumulative effect.

Using the full retrospective approach, the business recasts all comparative periods presented in the post adoption financial statements, according to Connor Group. In modified retrospective, the cumulative effect adjustment is flushed to retained earnings in the period of adoption for prior periods' effects. Cumulative effect has no restatement of comparative period amounts. Within those groupings lies the concept of the practical expedient. The standard prescribes accounting for an individual contract with a customer, but allows for application of the guidance to a portfolio of contracts with similar characteristics, if the entity thinks it wouldn't differ in effects on the financial statement.

In turn, **industries that typically haven't been subject to similar guidance** will need to comply with ASC 606. Companies have traditionally been

required to follow industry-specific guidance for revenue generating activities relating to the licensing, selling, leasing, hosting or marketing of products and services as specified in ASC 605 (and various preceding standards). These arrangements encompass multiple deliverables or elements: software and any combination of specified or unspecified enhancements, post-contract customer support, services and additional licenses.

Packaged software arrangements with multiple elements often have different dates of delivery (i.e. product and support), requiring accounting departments to recognize and defer revenue amounts appropriately. ASC 606 includes similar principles with the impact extending beyond the industries that have traditionally fallen under the guidance. Companies selling gadgets with accompanying services, including much of what falls into the "Internet of Things" category, are often considered as comparable contracts to those of software and services.

Finally, the mandate will have ripple effects that **extend beyond the finance department**—affecting everyone from manufacturing, to legal, to sales. No one line of business can operate in a vacuum.

EASING ASC 606 COMPLIANCE: ADVICE

MAXIMIZING PRACTICAL EXPEDIENTS

ASC 606 will have broad-reaching effects that extend beyond accounting processes—even having the ability to impact compensation tied to sales. Leveraging the revenue recognition automation features within NetSuite ensures seamless management and compliance, and allows you to focus time and energy on easing change management aspects of the new regulations—and ensuring organizational alliance. ASC 606 prescribes accounting for an individual contract with a customer, but allows for application of the guidance to a portfolio of contracts (or performance obligations) with similar characteristics. That allowance can take place if the entity reasonably expects that applying this guidance to the portfolio would not differ materially from applying this guidance to the individual contracts (or performance obligations) within that portfolio. Leveraging practical expedient methodology could result in process improvement as companies can limit the number of contract options, allowing sales to focus on selling and alleviating the myriad contract options that existed in the past.

BEING CLEAR ON PUBLIC DISCLOSURES

Above all, an **integrated system** eases this process. Many best-of-breed solutions in the marketplace promise to ease ASC 606 compliance, but bolting on additional technology only increases complexity and leaves information in silos, making it harder to ensure the transparency ASC 606 aims to accomplish. It won't leave your business with the agility to accommodate value-based or usage-based subscriptions. On the other hand, a core-unified framework connects transactions, subscriptions and projects to the billing engine, and seamlessly flows to financials, with full integration to advanced revenue management.

RUN SEAMLESS BILLING AND REVENUE RECOGNITION IN THE CLOUD

As if changing revenue recognition and compliance standards weren't enough, most industries are shifting to recurring revenue and sales models, which in turn impacts billing, collections and revenue recognition. Ensuring compliance and easing complexity relies on streamlining processes, which demands an end-to-end view of billing through the revenue recognition process.

NetSuite's Revenue Recognition Functionality

Even in this changing landscape, NetSuite makes ASC 606 compliance easy. For example, NetSuite supports recipes—i.e. the ability to automate how revenue is to be recognized on a contract. Recipes act in a similar fashion to how accounting systems depreciate a fixed asset—for example, using straight-line depreciation, accounting systems would take the cost of the fixed asset and divide it by the number of years in its useful

life and automate the recording of depreciation expense and accumulated depreciation. With NetSuite, recipes are used in a similar fashion—determine how revenue components of a contract are to be recognized, apply a rev rec recipe and press the button—it's that simple.

We do this through SuiteBilling, the industry's first and only comprehensive cloud solution that synchronizes complex processes from order to billing to revenue recognition, all within one system—an agile and sophisticated solution that offers unparalleled control and flexibility over billing and revenue management. SuiteBilling's centralized and future-proof framework supports the universe of monetization models and allows customers to be nimble, innovate rapidly and profit in today's marketplace. It unifies both billing and rev rec processes with complete controls and auditability to ease compliance while reducing risk. Built into NetSuite's core ERP system, SuiteBilling delivers unmatched functionality and business value.

NetSuite's unified system can manage orders from multiple sales channels, and manage billing and revenue recognition to support compliance with revenue recognition rules such as revenue arrangements with multiple elements (ASC 605-25) and percentage-of-completion accounting (ASC 605-35), while providing a foundation to prepare for adopting ASC 606. Additionally, NetSuite's cloud-based architecture, with the flexible and powerful SuiteCloud development platform, enables customizations that carry forward automatically with every upgrade and provides a robust ecosystem of complementary solutions.

When a contract exists for a vendor to perform multiple revenue-generating activities, the contract price for such arrangements has to be allocated and measured in alignment with revenue recognition standards. Industry guidance states how and when to separate elements within an arrangement for the performance or delivery of multiple products or services that occur over different points in time. NetSuite provides robust and comprehensive configurable capabilities based on requirements of ASC 605 and ASC 606/IFRS 15, enabling systematic compliance for complexities associated with accurately managing revenue contracts.

LET'S LOOK AT SOME KEY FEATURES:

- Flexible Revenue Contracts – Drive an agile and accurate view of the revenue contract. Revenue Arrangements are containers for Revenue Elements (performance obligations). Elements have individual attributes such as revenue rule, revenue plan start and end dates, and revenue allocated amount. Revenue Elements can be merged across linked orders or contracts, or split into multiple Arrangements, to accurately represent the revenue contract regardless of how the revenue source transactions are managed and billed.

- Dynamic Fair Value Pricing – Define the fair value as either a constant or a dynamic formula. Formulas can be based on information within other revenue elements—for example, a fair value for support based on a percentage of licenses within that contract. Item Revenue Groups allow for items with identical fair value requirements to share Fair Value Prices and eliminate duplication. The ability to add user defined dimensions allows a single item (or group of items) to have multiple Fair Value Prices and meet stratification requirements.

- Advanced Revenue Management and Billing Together – From consolidated invoicing, flexible pricing and packaging and automated rating processes, to seamless integrations with NetSuite Advanced Revenue Management and Core Financials modules, NetSuite SuiteBilling provides transparency around all billing activities with a powerful Software-as-a-Service (SaaS) suite. Unlike most products, Billing and Revenue Recognition are not integrated at NetSuite—they are built as one. Both the billing and revenue recognition modules use the same rating engine—built together to work together. This ensures that billing and revenue recognition never get out of sync—which is an inherint risk when you integrate different products together. Both built into the core ERP Suite, and built together using the same rating engine—unparalled in the market.

- Powerful Allocation Calculator – Leverage Fair Value Prices to automatically allocate arrangement consideration across all Elements within the Arrangement—including support for ASC 605 and ASC 606/IFRS 15 standards

- Support Percentage-of-Completion Accounting – Support revenue accounting for projects leveraging percentage-of-completion mechanisms.
- Support Event-Driven Revenue Plans – Align revenue recognition with event triggers—for example, the fulfillment of an item, the generation of a bill against an order or work beginning on a project. A single performance obligation can be associated with multiple plans in order to support partial fulfillments or billings.
- Revenue Recognition in Accordance with Multiple Accounting Standards – The globalization of business today is powered by several factors, including global capital markets, foreign direct investment and economic interdependence. In order to report financial results accurately within revenue recognition mandates based on multiple accounting standards (e.g. GAAP, IFRS), accounting departments worldwide can leverage a powerful Multi-Book Accounting engine that can record and post revenue-related activity to all books concurrently eliminating data entry replication and manual intervention.

Are you ready for what's next? NetSuite provides a nimble and sophisticated solution that offers unparalleled control and flexibility over billing and revenue management processes. SuiteBilling is a centralized and future-proof framework that supports the universe of monetization models and allows customers to be nimble, innovate rapidly and profit in today's marketplace. It is the first and only comprehensive cloud solution in the market today that synchronizes complex processes from order to billing to revenue recognition all within one system.

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