ACCOUNTING

Changes to revenue recognition in the consumer products industry

In May 2014, the Financial Accounting Standards Board issued new revenue recognition guidance that replaces most pre-existing revenue recognition guidance, including industry-specific guidance, in U.S. generally accepted accounting principles (GAAP). All entities in the consumer products (CP) industry whose financial statements are prepared in accordance with U.S. GAAP will be affected by the new guidance. To assist in understanding how a CP entity could be significantly affected by the new guidance, we have prepared a white paper, Changes to revenue recognition in the consumer products industry, in which we discuss the following topics, among others:

- Shipping and handling activities
- Warranties
- Customer options for additional goods or services (including customer loyalty programs)
- Volume and early payment discounts and rebates
- Rights of return (including restocking fees and costs)
- Price concessions
- Slotting fees, cooperative advertising and coupons
- Whether revenue should be recognized over time or at a point in time
- When control of a promised good or service transfers to a customer
- Sales involving resellers and consignment sales
- Bill-and-hold arrangements
- Principal vs. agent considerations
- Fulfillment costs related to customer contracts and the costs to obtain such contracts
- Disclosure requirements
While the effective dates for the new guidance are staggered, they are now upon us. With limited exceptions, the new guidance was effective as of January 1, 2018 for public entities with calendar year ends. For all nonpublic entities with calendar year ends, the new guidance is effective in the year ending December 31, 2019. Time is of the essence for these entities given that implementation of the new guidance could represent a significant undertaking in many cases. Our white paper can be a valuable tool in the implementation process to help understand the application of ASC 606 to your customer contracts.

Also, for comprehensive discussion and numerous examples of applying the new guidance, refer to our publication, A guide to revenue recognition.

Private company accounting for common control arrangements

As a result of the Private Company Council’s activities, the Financial Accounting Standards Board (FASB) has issued two Accounting Standards Updates (ASUs) to simplify the accounting for variable interest entities (VIEs) under common control.

On March 20, 2014, the FASB issued ASU 2014-07, Consolidation (Topic 810): Applying Variable Interest Entities Guidance to Common Control Leasing Arrangements. This ASU introduced an accounting alternative for private companies that, if elected, simplifies and reduces the costs of accounting for certain common control leasing arrangements.

On October 31, 2018, the FASB issued ASU 2018-17, Consolidation (Topic 810): Targeted Improvements to Related Party Guidance for Variable Interest Entities. This ASU effectively expands the private company accounting alternative for common control leasing arrangements to all private company common control arrangements as long as both the parent and the legal entity being evaluated for consolidation are not public business entities.

Under the new guidance, a private company may elect not to apply the complex VIE model in Topic 810, “Consolidation,” of the FASB’s Accounting Standards Codification to arrangements between legal entities under common control (including common control leasing arrangements) if certain criteria are met. If the private company accounting alternative is elected, a reporting entity should continue to apply other consolidation guidance unless another scope exception applies. Additionally, a reporting entity that elects the private company accounting alternative is required to provide certain detailed disclosures.

Both ASUs require retrospective adoption with a cumulative-effect adjustment to retained earnings at the beginning of the earliest period presented. ASU 2014-07 can be elected in any future period until the adoption of ASU 2018-17, and early adoption of ASU 2018-17 is permitted.

Determining whether to elect the alternative requires an evaluation of financial statement user needs, consideration of the probability of becoming or being acquired by a public business entity, and awareness of standard setter activities on consolidation. Our white paper, Private company accounting for common control arrangements, provides these and other insights.

Business combinations: In motion

RSM US LLP’s A guide to accounting for business combinations was developed to assist middle market companies in their application of Topic 805, “Business Combinations,” of the Financial Accounting Standards Board’s (FASB) Accounting Standards Codification (ASC). The third edition of the guide is currently available, and its content is based on information existing at June 1, 2016.

Given the continuing evolution of U.S. generally accepted accounting principles (including ASC 805), we have published a white paper, Business combinations: In motion, to highlight those standard-setting activities of the FASB that affect, or could affect, the content in the guide. Our white paper includes recent developments related to the new revenue, leasing and credit loss standards, as well as the impact of other standard-setting activities, such as the clarification of the definition of a business.
Market volatility: Consideration of goodwill impairment

As most people are aware, there was a great deal of volatility in the stock market during the last quarter of 2018. Whether or not an entity has adopted the private company accounting alternative for goodwill, impairment of goodwill needs to be considered when a triggering event occurs. Depending on the particular situation, a significant drop in share price could be such a triggering event. Therefore, it is important to document these goodwill impairment considerations if (a) the entity’s measurement period ends on a date other than December 31, 2018, or (b) the entity has elected the private company accounting alternative and it is more likely than not that the fair value of the entity (or reporting unit) is below its carrying amount.

Further information regarding the accounting for goodwill is available in our white papers:

- Simplifying the test for goodwill impairment
- Simplified accounting for private companies: Goodwill

FASB proposes targeted transition relief for CECL

In June 2016 the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, which introduced the current expected credit loss (CECL) model for the measurement of credit losses on financial assets measured at amortized cost basis, replacing the previous incurred loss methodology. ASU 2016-13 also modified the accounting for available-for-sale debt securities, which must be individually assessed, and expected credit losses recognized, when fair value is less than the amortized cost basis.

When analyzing the adoption of ASU 2016-13, some entities have decided to instead elect the fair value option in Subtopic 825-10, “Financial Instruments – Overall,” for some or all of their loan portfolios, which with limited exceptions, only is available for newly originated or purchased financial assets. These entities historically have measured their loan portfolios at amortized cost basis. The entities noted that, because of the limitations for when the fair value option can be elected, they would be required to maintain dual measurement methodologies (i.e., fair value for new assets and amortized cost for existing portfolios) that would result in noncomparable financial statement information for users.

To address these concerns, the FASB recently issued a proposed ASU, Targeted Transition Relief for Topic 326, Financial Instruments – Credit Losses, which, if finalized, would ease transition to the credit losses standard by providing the option to measure certain existing assets at fair value. Specifically, the proposed ASU would provide entities that have loans and other receivables within the scope of Subtopic 326-20, “Financial Instruments – Credit Losses – Measured at Amortized Cost,” with an option to irrevocably elect to account for assets within the scope of the fair value option guidance in Subtopic 825-10, “Financial Instruments – Overall,” at fair value through earnings. This election can be made on an instrument-by-instrument basis upon adoption of Topic 326, but cannot be made for debt securities, which the FASB decided to exclude from the scope of this transition relief.

The proposed ASU is available for comment until March 8, 2019.

SEC

SEC charges four companies with ICFR failures

On January 29, 2019, the SEC announced that it had settled charges against four public companies for failing to maintain internal control over financial reporting (ICFR) for seven to ten consecutive annual reporting periods. According to the SEC’s orders, year after year, the four companies disclosed material weaknesses in ICFR involving certain high-risk areas of their financial statement presentation. Each of
the four companies took months, or years, to remediate their material weaknesses after being contacted by the SEC staff. One of the companies is still in the process of remediating its material weaknesses.

Melissa Hodgman, an Associate Director in the SEC’s Enforcement Division, stated, “Companies cannot hide behind disclosures as a way to meet their ICFR obligations. Disclosure of material weaknesses is not enough without meaningful remediation. We are committed to holding corporations accountable for failing to timely remediating material weaknesses.”

**Critical audit matters: Audit committee perspectives**

In June 2017 the Public Company Accounting Oversight Board revised Auditing Standard 3101, *The Auditor’s Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion*, which requires auditors to communicate critical audit matters (CAMs) in their reports on audits of financial statements. The communication of each CAM in the auditor’s report will include public disclosure of information that heretofore has never been publicly released. This new requirement will have substantial ramifications for auditors and the companies they audit.

The Center for Audit Quality recently issued a video, *Critical Audit Matters: Audit Committee Perspectives*, in which audit committee chairs share their views on the significance of CAMs, steps they are taking as implementation of the standard nears, and implications for investors and others.

Our white paper, *Critical audit matters: Information for audit committees*, also is a resource for audit committee members who have questions about CAMs and the process for determining and disclosing them in the auditor's report.