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ASU 2014-09: Transition Requirements

By: **Ken Brackney**

Abstract

This blog entry highlights the transition requirements for ASU 2014-09, Revenue from Contracts with Customers. This ASU requires companies to apply the new guidance retrospectively, but permits a choice of two transition methods. Both transition methods offer some form of relief from the general requirements for retrospective application of a new accounting principle, stated in ASC 250-10-45-5 through 45-10. The first method is more in line with the general requirements, but it grants elective expedients that companies can use to ease the transition to the new standard. This method requires restating of comparative periods presented, but offers relief from full restatement and related disclosures in certain situations. The second method relieves companies from restating comparative periods, but still requires them to recognize and present the cumulative effect of retrospective application on the beginning retained earnings for the year of adoption.

Brackney, K. (2014). ASU 2014-09: Transition Requirements, NCACPA's website, posted September 29, 2014. NC Docks permission granted by author. Publisher version of record available at: https://www.ncacpa.org/blog/asu-2014-09-transition-requirements/

ASU 2014-09: Transition Requirements

September 29, 2014 • Accounting, ASU, Ken Brackney, Revenue

By: Ken Brackney
Blog Series: Revenue from Contracts with Customers

This blog entry highlights the transition requirements for ASU 2014-09, *Revenue from Contracts with Customers*. This ASU requires companies to apply the new guidance retrospectively, but permits a choice of two transition methods. Both transition methods offer some form of relief from the general requirements for retrospective application of a new accounting principle, stated in ASC 250-10-45-5 through 45-10. The first method is more in line with the general requirements, but it grants elective expedients that companies can use to ease the transition to the new standard. This method requires restating of comparative periods presented, but offers relief from full restatement and related disclosures in certain situations. The second method relieves companies from restating comparative periods, but still requires them to recognize and present the cumulative effect of retrospective application on the beginning retained earnings for the year of adoption.

Consider the following example: ABC Company, a public entity with a December 31 year-end, adopts ASU 2014-09 for its 2017 financial statements. ABC includes the comparative years 2016 and 2015 in these statements. ABC has one customer contract that is materially affected by adoption of the new standard. The table below shows the revenue patterns for this contract under the old and new guidance.

	2015	2016	2017
Revenue—Prior GAAP (the first method)	$100	$100	$100
Revenue—ASU 2014-09 (the second method)	$0	$240	$60
Difference	$100	–$140	$40

The contract runs from 2015 to 2017, and it has a fixed transaction price of $300. ASU 2014-09 requires companies to identify the *date of initial application*, in this case, January 1, 2017. The new standard defines a *completed contract* as one viewed as completed under the prior GAAP at the date of initial application. ABC's contract does not meet this definition.

The two transition methods differ mainly in how a company must present any comparative years. The first method requires retrospective application of the new standard, but permits three practical expedients. The procedure is described in ASC 606-10-65-1(d-g). Using the first method, ABC would need to restate the revenue and related items for 2016 and 2015. The related items might include expenses, such as bonuses and income taxes. In its 2017 comparative statements, ABC would need to show revenue from the contract of $0 in 2015, $240 in 2016 and $60 in 2017.

Applying the first method, ABC could elect from one to three practical expedients. Given the facts, ABC’s contract does not qualify for the first two expedients as they apply only to completed contracts. The first expedient permits companies to avoid restating the accounting for completed contracts that started and ended in the same year (2016 or 2015). The second permits companies with contracts involving variable consideration and affecting multiple periods to use the finalized transaction price for purposes of restating comparative periods. ABC could elect the third expedient, which permits companies to omit disclosure of the amount of any remaining performance obligations and the expected timing for recognition of this amount. ABC could elect to omit these disclosures for the restated 2016 and 2015 years. If a company elects any of the expedients, it must apply the election(s) consistently to all contracts and periods presented, and disclose the use of the expedient(s) and estimated effects.

ABC could opt for the second method instead. It follows the logic of an exception to the general guidance given in ASC 250-10-45-6, in which a company is relieved from restating comparative periods, but still must record and report the cumulative effect of the change in method on beginning retained earnings for the adoption year. The procedure is outlined in ASC 606-10-65-1(d and h-i). Companies need only consider the contracts not completed as of the date of initial application.

Applying the second method, ABC would continue to report revenue for 2015 and 2016 under the old guidance ($100 each year), and it would report $60 of revenue for 2017 under the new standard. The total revenue reported for the contract would be just $260. ABC would need to report the $40difference, as part of a cumulative effect adjustment to the retained earnings for January 1, 2017. Ignoring income taxes and other expenses that might change, ABC would need to present a $40 credit adjustment to the opening retained earnings. In addition, ABC would need to disclose the changes in other affected line items and the reasoning for any significant changes.

Method 2 is easier for companies to apply as they would need to evaluate just the open contracts at date of initial application. The first method offers the advantage of seeing all reported periods on the same basis.

So this wraps our multipart blog series on the new Rev Rec ASU. We hope you found the blogs informative!

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