

## OVERVIEW OF HOW ASC 606 IMPACTS CONSTRUCTION COMPANIES

ASC 606 is the revenue recognition standard that affects all businesses—including construction companies—that enter into contracts with customers to transfer goods or services. The standard is intended to provide an accounting framework for all businesses, whatever the industry, and make it easier for investors and others to compare your construction company's results with those of other construction companies as well as with companies in other industries.

ASC 606 sets out a standard five-step model for the revenue recognition process:

1. Identify the contract with the customer
2. Identify the performance obligations in the contract
3. Determine the transaction price
4. Allocate the transaction price
5. Recognize revenue when or as the entity satisfies a performance obligation

### FIVE STEPS TO CONTRACT COMPLIANCE

To make sure you're properly recognizing revenue under ASC 606, follow these steps in order:



Complying with ASC 606 requires reviewing every one of the company's existing contracts and setting a framework to follow for future contracts. It can be overwhelming.

The best place to start is by developing a rules-based framework for assessing your company's contracts. The framework needs to address:

- ▶ Whether to use full retrospective or the modified retrospective method. The full retrospective method requires restatement of the prior two (or three) comparative years, while the modified retrospective method requires dual recordkeeping during the adoption year. Each method has pros and cons, but both require significant effort.
- ▶ Treatment of quantitative and qualitative disclosures, including rules for systematically gathering, reviewing, and disclosing information about remaining performance obligations, resources consumed, labor hours expended, costs incurred and machine hours used.
- ▶ Developing post-transition rules for tracking performance obligations, multiple revenue streams, contract modifications, internal controls, and applying new revenue calculation rules.

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Accomplishing all of these tasks takes time and planning, in part because it reaches beyond the company's accounting and finance functions to include IT and HR:

- ▶ IT must be involved because its systems must be configured to (1) collect and analyze the information needed to produce acceptable disclosures, (e.g., for variable considerations) and (2) extract the information needed for judgment-based decisions.
- ▶ HR must be involved if, for example, the company has a bonus and compensation arrangement linked to revenue, such as bonuses for meeting or beating a contractual deadline.

Many of the reporting requirements under ASC 606 require contractors to use substantial judgment regarding how each contractual element should be reported. In addition, the calculations can be quite detailed and complex. Fortunately, software is available that will automate day-to-day revenue recognition tasks and regulatory compliance.

These reasons are why many companies opt to ask their advisors to review their decision-making processes and procedures and help them choose the software system that best meet their needs.

### HAVE QUESTIONS?

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