Implementing Revenue Recognition & NFP Reporting Model Changes for Behavioral Health Organizations

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Background & Key Principles
• Effective for Public Business Entities (& not-for-profit entities that are conduit debt obligors) in fiscal years & interim periods beginning after December 15, 2017

• Effective for all other entities in fiscal years beginning after December 15, 2018

• Principles based approach instead of a rules based approach
ASU 2014-09
REVENUE FROM CONTRACTS WITH CUSTOMERS

SCOPE OF NEW STANDARD
All entities that enter into contracts with customers:
• Public, private, not-for-profit
• Regardless of industry

EXCEPTIONS
• Lease contracts
• Insurance contracts
• Financial instruments
• Guarantees
• Non-monetary exchanges in the same line of business to facilitate sales to customers

EXCLUSIONS
• Contributions
• Collaborative agreements
Insurance Contract Exception

• Entities that fall under ASC 944: Financial Services – Insurance Entities are excluded

However…

• Entities that fall under ASC 954: Health Care Entities are in scope and so their insurance-related revenues need to be considered

• Arrangements seen within health care entities that are in-scope include the following examples:
  • Claims handling / ASO arrangements
  • Capitation & prepaid arrangements
ASU 2014-09
REVENUE FROM CONTRACTS WITH CUSTOMERS

- Areas of emphasis for healthcare:
  - Assessing credit risk for certain clients up-front
  - Portfolio rationalization and support
  - New allowance model design, build, review and calibration
  - Contract asset considerations
  - Disclosures: required and optional

- Other considerations
  - Alternative payment models
  - Supplemental payments
  - Capitation payments
NEW REVENUE RECOGNITION PROCESS

1. Identify Contract with a Customer
2. Identify Performance Obligations
3. Determine the Transaction Price
4. Allocate the Transaction Price
5. Recognize Revenue When/As a Performance Obligation is Satisfied
Step 1 – Identify the Contracts

• Identify the contracts with customers
  • Who are our customers & do we have contracts?
    • Focus on accounting not legal

• Characteristics of a contract
  • 2 parties = provider & patient/client
  • Enforceable rights & obligations = yes
  • What is the form? written/implied

• Criteria to recognize revenue from a contract
  • Approval & commitment – consent to treat, etc.
  • Commercial substance – provided care/labs/etc.
  • Probable of collection
    • Free care does not equal revenue – see transaction price later
Step 2 – Identify the Performance Obligation

• Identify the performance obligation
  • Distinct service – client care
  • Distinct good – prescription

• Capable of being distinct & distinct within the context of the contract
  • Global billing – Bundled payments, i.e., prenatal to delivery

• Current practice management systems handle the majority of the performance obligation tracking sufficiently
Step 3 – Determine Transaction Price

- Determine the transaction price
  - Amount of consideration to which the entity expects to be entitled

- Gross charges – explicit – implicit = transaction price

- Explicit price concessions
  - Reductions in accepted payment from your fee schedule based on an agreement with a third party or an internal organizational policy
    - Example - Contractual adjustments & self-pay discounts

- Implicit price concessions
  - Providers know they will not collect 100% of the remaining balance due
    - Example – Historically only collect x% of self-pay balance
• Bad debt expense
  • Limited/smaller balance due to implicit price concessions
  • Typically client/payor-specific event known to entity that suggests the client/payor no longer has ability & intent to pay amount due – represents impairment, like bankruptcy

<table>
<thead>
<tr>
<th>Location</th>
<th>Type</th>
<th>Example</th>
<th>Tracking</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Revenue</td>
<td>Gross Charge</td>
<td>Full Charge</td>
<td>Billing system</td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>Explicit Price Concession</td>
<td>Contractual</td>
<td>Billing system &amp;/or allowance methodology</td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>Implicit Price Concession</td>
<td>Self pay allowance</td>
<td>Billing system &amp;/or allowance methodology</td>
</tr>
<tr>
<td>Operating Expense</td>
<td>Bad Debt</td>
<td>Write-off</td>
<td>Billing system</td>
</tr>
</tbody>
</table>
STEP 3 – DETERMINE TRANSACTION PRICE

- Portfolios - practical expedient
  - Similarities to groupings for allowance calculation now
  - Common payor types with similar characteristics
  - Key – this approach would not differ materially from considering contracts individually
  - Consider separating self-pay into more classifications
    - Uninsured vs self-pay related to deductibles
Step 3 – Determine Transaction Price

• Example – Medicare Portfolio

Scenario:
• Medicare gross charges = $1.6 million
• Medicare contractual adjustments = $200,000
• Remaining balance
  • Medicare (100% collectible) = 80% of balance
  • Client (33% collectible) = 20% of balance

Recognizing Revenue:
• Gross Revenue = $1.6 million
• Explicit price concession = $200,000
• Remaining balance = $1.4m
• Client responsibility = $280,000 (20% of balance)
• Implicit price concession Client = $187,600
• Transaction Price
  • Medicare: $1,120,000
  • Self Pay: $92,400
Step 4 – Allocate Transaction Price

• Allocate the transaction price to the performance obligations
  • Only applies when multiple performance obligations exist
  • Practically significant when over more than one reporting period

• Performance obligations & gross charges easily identifiable based on charge master
  • May apply portfolio approach to similar performance obligations
Step 5 – Recognize Revenue

- Occurs when customer obtains control of the good or service
  - Client visit is performed/completed
  - Good is given: prescription

- Recognize revenue as performance obligations are satisfied
  - Not expected to result in any significant changes from revenue being recognized as procedures are performed (current methodology)

- Consideration of revenue cut-off
  - Close charts/visits timely from providers, record encounters on correct date, post payments on the date they are received
Example Timeline & Process Considerations
WHAT TO DO NOW?

1. Read the standard & related resources
2. Identify a champion or task force to study the new standard and reiterate project timeline
3. Determine if resource bandwidth & competencies exist within the organization or if outside assistance is needed
4. Engage Reimbursement, IT, & Finance staff (& third party, if deemed necessary)
5. Identify revenue streams & the related portfolios
6. Concentrate on disclosures & if any changes are needed to gather the information
7. Educate audit committees, boards, and other stakeholders
Assessment is based on both the customer’s ability & intent to pay as amounts become due. No such thing as cash basis.

**KEY SUCCESS FACTORS:**

- Starting near implementation is critical - Don’t underestimate the time and resources needed for a successful adoption.
- Document timeline and build consensus from all stakeholders – delays could lead to surprises in the audit process.
- Engage auditors early; learn from others’ adoption successes and challenges so they can provide insight.
- Take advantage of BKD’s Thoughtware & on-site education event.
- Consult frequently with auditors to avoid surprises later.

**TO DO’S**
ADOPTION TIMELINE TO AVOID SURPRISES

1. 2018 FINANCIAL STATEMENT CLOSE
2. REVENUE SCOPING
3. ANALYSIS OF IN-SCOPE REVENUES INCLUDING CONTRACT REVIEW & PORTFOLIO SELECTION. DEVELOP PRELIMINARY CONCLUSIONS
4. DOCUMENT FINAL ANALYSIS AND CONCLUSIONS
5. AUDIT OF ADOPTION & SIGNOFFS OFF ON ACCOUNTING CONCLUSIONS
6. DEVELOP NEW QUARTERLY AND ANNUAL DISCLOSURES; RECORD ADOPTION ENTRY AND DRAFT NEW FINANCIAL STATEMENT PRESENTATION
7. 2019 FINANCIAL STATEMENT CLOSE

TO-DO’S (FROM PREVIOUS SLIDE)

1. 2018 FINANCIAL STATEMENT CLOSE
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7. 2019 FINANCIAL STATEMENT CLOSE

Adoption Date

Fall 2018 | Q1 FY2019 | Q2 FY2019 | Q3 FY2019 | Q4 FY2019 | FY 2020
REVENUE SCOPING

KEY SUCCESS FACTORS:

• Identify all revenue by starting with trial balance
• For each revenue general ledger account, document whether in-scope or not-in-scope
  • Not in scope items could include rental income or insurance revenue, which are specifically excluded from Topic 606
• Materiality considerations
  • Standard does not apply a materiality concept so care should be given to ensure insignificant items are not significant in the aggregate
• Goal to have auditor “sign-off” on scoping by end of Q1 or early Q2 of FY2019
KEY SUCCESS FACTORS:

- Evaluation & documentation of contract terms is critical (5 step model); Contract analysis documentation should be agreed-upon up-front
- Analysis of portfolio(s) & the related portfolio rationalization involves judgment and verification
- For in-scope items, consider level of analysis and documentation needed
  - High: Large and complex revenue streams
  - Low: Revenue that is non-complex (e.g., cafeteria revenue)
  - Medium: Judgment will be needed
- Engage auditors along the way; frequent touch-points are important
- Don’t wait until end of project to select adoption method
KEY CLIENT SUCCESS FACTORS:

- Schedule touch-points to evaluate progress, initial conclusions, and discuss judgments and challenges
- Build consensus with team members and auditors early on level of documentation for each revenue stream
- Goal to have auditors “sign-off” on all key adoption concepts in Q3 of FY2019
  - Having this creep into Q4 will increase risk of surprises and could cause bandwidth issues
KEY SUCCESS FACTORS:

- Co-develop date by which auditors will receive all final items to audit
- Consider technical consultation throughout the year
  - Reduces risk of surprises by building consensus along the way
  - Does not alleviate need for audit through direct testing (review of contracts, etc.)
  - Plan ahead for this testing by having contracts and other support ready
- Goal to have auditors “sign-off” on all auditing in early Q4 of FY2019
  - Disclosures could be a significant undertaking so finalizing the accounting in this time frame is critical to allow sufficient time to build disclosures
Assessment is based on both the customer’s ability & intent to pay as amounts become due.

No such thing as cash basis.

**KEY SUCCESS FACTORS:**

- Discuss adoption method selection early in the process.
- Recognize early that the new disclosure requirements are significant and will take time to develop; Understand early the nature of the requirements and what system and process changes may be necessary to accumulate the disclosures.
- Goal to have auditors “sign-off” on financial statement presentation and disclosure format by end of calendar FY2019.
Transition Methods & Guidance
## Transition Approaches

<table>
<thead>
<tr>
<th>Transition Approach</th>
<th>2017</th>
<th>2018</th>
<th>Date of Cumulative Effect Adjustment*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Full Retrospective</td>
<td>Restate for all contracts</td>
<td>Apply to all contracts</td>
<td>January 1, 2017</td>
</tr>
<tr>
<td>Full Retrospective Using One or More Practical Expedients</td>
<td>Restate for all contracts except contracts covered by practical expedients</td>
<td>Apply to all contracts</td>
<td>January 1, 2017</td>
</tr>
<tr>
<td>Modified Retrospective</td>
<td>No contracts restated; reported based on legacy guidance</td>
<td>Apply to all contracts</td>
<td>January 1, 2018</td>
</tr>
</tbody>
</table>
Methods of Adoption - Terms

• Disclosure required for change in accounting principle
  • Nature & reason for change
  • Method for applying change

• Date of initial application = start of reporting period of first application

• Completed contract = contract for which all (or substantially all) of the revenue was recognized before the date of initial application
Methods of Adoption - Example

- December 31, 2019 fiscal period end – non-public entity
- Date of initial application = January 1, 2019
- Completed contract = contract for which all (or substantially all) of the revenue was recognized before January 1, 2019
Full Retrospective Method – Practical Expedients

- For completed contracts, do not need to restate contracts that begin & end within the same annual reporting period.
- For completed contracts that have variable consideration, an organization may use the transaction price at the date the contract was completed rather than estimating variable consideration amounts in the comparative reporting periods.
- For all reporting periods presented before the date of initial application, an organization need not disclose the amount of the transaction price allocated to remaining performance obligations & an explanation of when the organization expects to recognize that amount as revenue (comparative disclosures).
For any practical expedients used, they should be applied consistently to all contracts within all reporting periods presented.

Disclose effect of changes on comparative reporting periods only.

Disclose expedients that have been used & to the extent reasonably possible, a qualitative assessment of the estimated effect of applying each expedient.
Modified Retrospective Method

- Recognize cumulative effect of initial application as an adjustment to beginning unrestricted net assets for the annual reporting period of initial adoption.

- Option to elect to apply to all contracts at date of initial application or only to contracts not completed at the date of initial application:
  - Disclosure required
  - Same option & disclosure requirements as full retrospective method regarding contracts modified before the beginning of the earliest reporting period presented.
Understand the Impact Then Your Options

• What are your revenue streams?
• Which revenue streams, if any, will require restatement?
• Would presenting a single year financial statement reduce implementation time & complexity?
• Consider choosing the option that meets the needs of the Organization & the user of the financial statements with the least amount of work
COMMON QUESTIONS IN ADOPTION

1. Do we need any new systems? Will our general ledger change?

2. Will we have any bad debt expense?

3. What about cut-off at period end?

4. Who should be involved in the implementation process?

5. How does this standard change the IRS Form 990, community benefit reporting & the cost report requirements?
Common Industry Implementation Challenges
AICPA REVENUE RECOGNITION TASK FORCES

- Develop a new Accounting Guide on Revenue Recognition
- Guide to provide helpful hints & illustrative examples on how to apply the standard
- Guidance will not be prescriptive but instead is intended to be a resource
- Full implementation issues are posted for comment after review from the overall Revenue Recognition Working Group & FinREC
- List of issues for the health care industry is posted on the AICPA website

HEALTH CARE ISSUES IDENTIFIED BY THE AICPA REVENUE RECOGNITION TASK FORCE

Issues Identified & Finalized:

• Revenue recognition for self-pay (application of Steps 1 & 3)
• Application of the portfolio approach
• Disclosure requirements
• Third-party estimates
• Bundled payments & risk sharing arrangements

Issues Identified & Open:

• Contract acquisition costs
  • Final paper to be presented to FIN Rec in September of 2018
• Identifying the performance obligation & recognition of refundable & non-refundable entrance fees for CCRC’s, including significance financing component considerations and future service obligations
  • Final paper to be presented to FIN Rec in September of 2018
What should we consider?

Customary business practice of not performing a credit assessment prior to providing services

Continues to provide services to a client even when historical experience indicates that it is not probable that the entity will collect substantially all of the discounted charges (gross or standard charges less any contractual adjustments or discounts) in the contract.
FinREC believes that the health care entity has implicitly provided a price concession to the client, even if it will continue to attempt to collect the full amount of discounted charges.
Do we reassess?

An entity is required to update the estimated transaction price at the end of each reporting period. If an entity experiences subsequent adjustments that result in decreases to client revenue, the entity should re-assess whether its estimation process is appropriate.
FinREC believes that changes in the entity’s expectation of the amount it will receive from the client will be recorded in revenue unless there is a client-specific event that is known to the entity that suggests that the client no longer has the ability & intent to pay the amount due & therefore the changes in its estimate of variable consideration better represent an impairment (bad debt).
BAD DEBT EXPENSE

So when would there be bad debt expense?

When a health care entity performs a credit assessment prior to providing services to a client & expects to collect substantially all of the discounted charges.

What's the impact?

For example, an elective procedure in which historical experience supports collection of substantially all of the discounted charges.
Many health care providers expect a **significant decrease** in the provision for bad debts for services provided to uninsured & insured clients with co-payments & deductibles, in comparison to what is currently recorded under U.S. GAAP.
PORTFOLIO APPROACH

Entities can apply the standard to a portfolio of contracts or performance obligations with similar characteristics.

Entities must reasonably expect that the financial statement effect of using the portfolio approach will not differ materially from applying the standard on a contract-by-contract basis.

Key considerations

- How to apply a portfolio approach
- How to establish portfolios
- How to determine effect would not differ materially
PORTFOLIO APPROACH

More on key considerations:

• Portfolio approach may be applied to all aspects of the model or only to certain steps

• If establishing portfolios, an entity will need to use judgment to determine the size, composition & number of portfolios
  • Health care entities may consider segregating by payor class, type of service & other categories

• An entity also will need to consider materiality & documentation requirements
• Considerations for a health care entity to determine in grouping contracts with similar characteristics for inclusion in a portfolio:
  • Type of service
  • Type of payors – e.g., insurance, governmental program, self-pay
  • Whether contracts are entered into at or near the same time
• A health care entity may include some or a combination of the above considerations in its determination of a portfolio
• A health care entity may reclassify the remaining self pay balance (co-pay or deductibles) into a separate portfolio after insurance company has paid
Disclosure Considerations
## Required Disclosures – Public vs. Non-Public

<table>
<thead>
<tr>
<th>Disclosure Description</th>
<th>Public</th>
<th>Non-Public</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Contracts with clients (customers) – Revenue recognized (client services revenue or other) &amp; impairment loss (bad debt), separated from other sources of revenue (grants, contributions, etc.)</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>a. Disaggregation of revenue – Categories that depict the nature, amount, timing &amp; uncertainty of revenue &amp; cash flows (like payer type – Medicaid, Medicare, etc.)</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>b. Disaggregation of revenue – Revenue recognized based on timing of satisfaction of performance obligations; Qualitative information about economic factors affecting the nature, amount, timing &amp; uncertainty of revenue &amp; cash flows (narrative rather than #s)</td>
<td>N/A</td>
<td>Yes, unless elect 1.a.</td>
</tr>
<tr>
<td>c. <strong>Contract balances – Opening &amp; closing balances of receivables, contract assets &amp; liabilities</strong></td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>d. Contract balances – Revenue recognized that was included in the contract liability at the beg. of the reporting period; Correlation between timing of satisfaction of performance obligations &amp; typical timing of payment; Cause of significant changes in contract asset &amp; liability balances</td>
<td>Yes</td>
<td>No</td>
</tr>
</tbody>
</table>
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<tr>
<th>Disclosure Description</th>
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<tbody>
<tr>
<td>1. Contracts with clients</td>
<td></td>
<td></td>
</tr>
<tr>
<td>e. Performance obligations – Timing of satisfaction of performance obligations; Significant payment terms; Nature of goods/services; (obligations for returns, refunds, types of warranties)</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>f. Performance obligations – Aggregate transaction price allocated to unsatisfied performance obligations; Revenue recognized for performance obligations satisfied in previous periods; Expected timing of recognition of revenue for unsatisfied performance obligations (consider which performance obligations cross financial periods affecting this disclosure)</td>
<td>Yes</td>
<td>No</td>
</tr>
</tbody>
</table>
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<th>Non-Public</th>
</tr>
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<tbody>
<tr>
<td>2. Significant judgments – Judgments &amp; changes in judgments that significantly affect the amount &amp; timing of revenue</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>a. For performance obligations satisfied over time, method used to recognize revenue</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>b. For performance obligations satisfied over time, explanation on how methods used faithfully depict the transfer of goods/services</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>c. For performance obligations satisfied at a point in time, significant judgments made in evaluating when a customer obtains control</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>d. Methods, inputs &amp; assumptions used for determining transaction price &amp; allocating the transaction price</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>e. Methods, inputs &amp; assumptions used for assessing whether an estimate is constrained (think AR allowance &amp; 3rd party estimates)</td>
<td>Yes, unless elect 2.d.</td>
<td>Yes</td>
</tr>
</tbody>
</table>
## Required Disclosures – Public vs. Non-Public

<table>
<thead>
<tr>
<th>Disclosure Description</th>
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<th>Non-Public</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>2. Significant judgments</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>f. Amount of sliding fee adjustments &amp; implicit price concessions (not required, may quantify community benefit)</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>g. Methods, inputs &amp; assumptions used for measuring obligations for returns, refunds &amp; similar obligations</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td><strong>3. Assets arising from costs to obtain or fulfill a contract</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Judgments made in determining amount of cost incurred &amp; method used to determine amortization</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>b. Closing balances &amp; amount of amortization &amp; impairment losses</td>
<td>Yes</td>
<td>No</td>
</tr>
</tbody>
</table>
## Disaggregation of Revenue – By Service Line & Timing

The composition of patient care service revenue based on the Organization’s lines of business and timing of revenue recognition for the years ended December 31, 2019 and 2018 is as follows:

<table>
<thead>
<tr>
<th>Health care services transferred over time:</th>
<th>2019</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Medical</td>
<td>$ 3,730,000</td>
<td>$ 3,520,000</td>
</tr>
<tr>
<td>Dental</td>
<td>2,850,000</td>
<td>2,750,000</td>
</tr>
<tr>
<td>Behavioral health</td>
<td>1,650,000</td>
<td>1,570,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$ 8,230,000</strong></td>
<td><strong>7,840,000</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Pharmacy sales at point in time</th>
<th>2019</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2,080,000</td>
<td>1,960,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$ 10,310,000</strong></td>
<td><strong>$ 9,800,000</strong></td>
</tr>
</tbody>
</table>
Quantitative & Qualitative Disclosures
  • Contracts with Customers
  • Significant Judgements
  • Assets Recognized

Level of Detail
  • Need enough to explain, not so much it confuses

Performance Obligations
  • Over time or a Point in time

Transaction price
  • Allocation & subsequent changes
  • Optional disclosures
    • Implicit price concessions
Accounting Guidance for Contributions Received & Contributions Made
Contributions & Grants

- One June 21, 2018, the FASB Issued ASU 2018-08, Clarifying the Scope & the Accounting Guidance for Contributions Received & Contributions Made

- The ASU clarifies:
  - Whether an asset transfer is a contribution or an exchange transaction
  - The criteria for determining whether contributions are unconditional (& recognized immediately into income) or conditional (& deferred)
The final standard should be applied on a modified prospective basis following the effective date to agreements that are either (a) incomplete as of the effective date or (b) entered into after the effective date. Retrospective application is permitted.

Resource providers have an additional year to implement the provisions on the standard.

1 – Public entities include NFPs with conduit debt obligations
Exchange Transaction
If commensurate value is received by the resource provider, the transaction should be accounted for as an exchange transaction by applying ASC 606 or other topics.

Contribution Transaction
If commensurate value is not received by the resource provider, i.e., the transaction is nonexchange, the recipient organization would record the transaction as a contribution under ASC 958 & determine whether the contribution is conditional or unconditional.
Where to Start

Framework for Classifying Transfers of Assets

Is the transaction one in which each party directly receives commensurate value?
- Yes: It is an exchange transaction. Apply Topic 606 on revenue from contracts with customers or other applicable topics.
- No:
  - Yes: Is the payment from a third-party payer on behalf of an existing reciprocal transaction?
    - Yes: It is a balance-sheet only transaction. No effect on an entity’s revenue recognition.
    - No: It is a nonreciprocal transaction. Apply contribution (non-exchange) guidance.
  - No: Are there conditions present (a barrier and a right of return/right of release must exist)?
    - Yes: Are restrictions present (that is, limited purpose or timing)?
      - Yes: It is unconditional and with donor restrictions.
      - No: It is unconditional and without donor restrictions.
    - No: It is unconditional. Recognize revenue in appropriate net asset class.

Meeting of Condition
Exchange vs. Nonexchange Transactions

*The revenue recognized is the underlying contract with the client*
CONTRIBUTIONS: CONDITIONAL OR UNCONDITIONAL?

Organizations would evaluate whether contributions ("nonexchange" transactions) are conditional or unconditional by determining whether there is a barrier or hurdle that must be overcome & whether the agreement or other referenced document includes either a right of return of assets transferred or a right of release of a promisor's obligation to transfer assets.

To determine if there is a barrier, an NFP will consider indicators, which include, but are not limited to:

- The inclusion of a measurable performance-related barrier or other measurable barrier
- The extent to which a stipulation limits discretion by the recipients on the conduct of an activity
- The extent to which a stipulation is related to the purpose of the agreement
Simultaneous Release Option

The ASU modifies the current simultaneous release option, which allows an NFP to recognize a restricted contribution directly in unrestricted net assets/net assets without donor restrictions if the restriction is met in the same period that the revenue is recognized.

This election may now be made for all restricted contributions that were initially classified as conditional without having to elect it for all other restricted contributions & investment returns.
## Example

<table>
<thead>
<tr>
<th>Block Grants</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Typically paid 1/12 per month</td>
</tr>
<tr>
<td>• Current treatment - revenue recognized monthly as grant revenue</td>
</tr>
<tr>
<td>• New treatment – barrier to overcome + right to return = conditional contribution - revenue recognized monthly</td>
</tr>
<tr>
<td>• No change in internal accounting and no required change to financial statement presentation on statement of operations</td>
</tr>
</tbody>
</table>
Example

- Federal grant received in advance
  - Organization is awarded grant of $100,000, and receives all funds in advance
  - Current treatment – recorded as deferred revenue initially, and revenue is recognized over the grant period as organization has qualified expenditures.
  - New treatment – if the Federal agency is not receiving commensurate value, organization recognizes $100,000 as revenue with restriction when the grant is awarded. Net assets with donor restrictions are released as the funds are properly spent in accordance with the grant agreement.
Other Revenue Streams
Pharmacy Revenue
Pharmacy Revenue in Five-Step Model

1. Contracts with client to fill prescription written by provider & filled by pharmacy (in-house or contract)
2. Dispensation of each distinct drug
3. Retail price – explicit price concessions – implicit price concessions = collections from client & third party
4. Allocate transaction price among drugs based on collections from client & third party for each drug
5. Recognize revenue when prescription is filled
Presentation & Disclosure of Pharmacy Revenue

• No change in presentation
  • Client accounts receivable on balance sheet
  • Client care service revenue on statement of operations
  • In contract pharmacy relationships, dispense fee, admin fee & drug cost are excluded from guidance & should be expense

• Disclosure of revenue recognized over time vs. point in time
  • Essentially a disclosure of pharmacy revenue disaggregated from other service lines (medical, dental, etc.)
Bundled Payment
BUNDLED PAYMENT ARRANGEMENTS

Step 1 | Identification of The Contract
FinREC believes the contract is with the patient not the third party payer

Step 2 | Performance Obligation
Care Coordination is not necessarily a performance obligation. Need to assess each contract & in addition consider implied promises & if so are they a distinct performance obligation

Step 3 | Transaction price considerations
• Variable consideration
• Constraint of revenue
• Use of portfolios
• Significant financing component
• Do you have historical information to estimate the variable consideration
• Exposed an example for CJR
IMPLEMENTING THE NEW NOT-FOR-PROFIT REPORTING MODEL
• Effective for financial statements for fiscal years beginning after December 15, 2017, & for interim financial statements for periods after that date (early adoption is allowed)

• If comparative financial statements are issued, NFP may omit the following information in comparative financial statements for any years presented before the adoption year
  • Analysis of expense by functional & natural classification
  • Disclosures around liquidity & availability of resources
Net Asset Classification Scheme

- Current GAAP
  - Unrestricted
  - Temporarily restricted
  - Permanently restricted

- Updated GAAP
  - Without donor restrictions
  - With donor restrictions
## Required Disclosures for Net Assets Classification Scheme

<table>
<thead>
<tr>
<th>Without Donor Restrictions</th>
<th>With Donor Restrictions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amounts &amp; purpose of governing board designations</td>
<td>Composition of net assets at period’s end</td>
</tr>
<tr>
<td>Can be disclosed on face or in the notes</td>
<td>How the restrictions affect resource use</td>
</tr>
<tr>
<td></td>
<td>Can be disclosed on face or in notes</td>
</tr>
<tr>
<td></td>
<td>2018</td>
</tr>
<tr>
<td>--------------------------------------</td>
<td>------</td>
</tr>
<tr>
<td><strong>Net Assets</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Net Assets Without Donor Restrictions</strong></td>
<td></td>
</tr>
<tr>
<td>Board-designated</td>
<td>-</td>
</tr>
<tr>
<td>Undesignated</td>
<td></td>
</tr>
<tr>
<td><strong>Total Net Assets Without Donor Restrictions</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Net Assets With Donor Restrictions</strong></td>
<td></td>
</tr>
<tr>
<td>Perpetual in nature</td>
<td>-</td>
</tr>
<tr>
<td>Purpose restriction</td>
<td></td>
</tr>
<tr>
<td>Time-restricted for future periods</td>
<td></td>
</tr>
<tr>
<td><strong>Total net assets</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Total liabilities and net assets</strong></td>
<td>$</td>
</tr>
</tbody>
</table>
### Example

#### STATEMENTS OF OPERATIONS

<table>
<thead>
<tr>
<th>Revenue and support without donor restrictions</th>
<th>2018</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Subcapital premium revenue</td>
<td>$</td>
<td>$</td>
</tr>
<tr>
<td>Net client service revenue</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Other</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Net assets released from restrictions</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total revenues and support without donor restrictions</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Expenses</th>
<th>2018</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personnel</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Client related</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Occupancy</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Operating</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Donated items</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Total expenses</strong></td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Operating Income (Loss)</th>
<th>2018</th>
<th>2017</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>Other Income (Expense)</th>
<th>2018</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investment return</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Gain on investment in equity investees</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Excess (Deficiency) of Revenues Over Expenses</th>
<th>2018</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investment return - change in unrealized gains and losses on other than trading securities</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Net assets released from restriction used for purchase of property and equipment</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Increase (Decrease) in Net Assets Without Donor Restriction</th>
<th>2018</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$</td>
<td>$</td>
</tr>
<tr>
<td></td>
<td>2018</td>
<td>2017</td>
</tr>
<tr>
<td>-----------------------------</td>
<td>------</td>
<td>------</td>
</tr>
<tr>
<td><strong>Changes in Net Assets Without Donor Restrictions</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Excess (deficiency) of revenues over expenses</td>
<td>$</td>
<td>$</td>
</tr>
<tr>
<td>Investment return - change in unrealized gains and losses on other than trading securities</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Net assets released from restriction used for purchase of property and equipment</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Increase (decrease) in net assets without donor restrictions</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Changes in Net Assets With Donor Restrictions</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contributions received</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Investment return</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Net assets released from restriction</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Increase (decrease) in net assets with donor restrictions</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Change in Net Assets</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Net Assets, Beginning of Year</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Net Assets, End of Year</strong></td>
<td>$</td>
<td>$</td>
</tr>
</tbody>
</table>
## Net Assets With Donor Restrictions

Net assets with donor restrictions are available for the following purposes or periods:

<table>
<thead>
<tr>
<th></th>
<th>20X2</th>
<th>20X1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Subject to expenditure for specified purpose</td>
<td>$</td>
<td>$</td>
</tr>
<tr>
<td>Purchase of equipment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Indigent care</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Health education</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subject to the passage of time</td>
<td></td>
<td></td>
</tr>
<tr>
<td>For periods after ______________, ___</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Endowments</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subject to spending policy and appropriation</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investments to be held in perpetuity, the income is expendable</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subject to appropriation and expenditure when a specified event occurs</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Endowment requiring income to be added to the original gift until fund value is $________</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Not subject to appropriation or expenditure</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Beneficial interests in perpetual trusts</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Beneficial interests in assets held by Model Hospital Foundation</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>$_______</td>
<td>$_______</td>
</tr>
</tbody>
</table>
### Net Assets Released from Restrictions

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of the passage of time or other events specified by donors.

<table>
<thead>
<tr>
<th></th>
<th>20X2</th>
<th>20X1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purpose restrictions accomplished</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchase of equipment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Indigent care</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Health education</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Time restrictions expired</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Passage of specified time</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Release of appropriated endowment amounts without purpose restrictions</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Release of appropriated endowment amounts with purpose restrictions</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total restrictions released</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

$______  $______
Board-designated net assets

• New FASB ASC master glossary definition:
  • Net assets without donor restrictions subject to self-imposed limits by action of the governing board
  • Board designated net assets may be earmarked for future programs, investment, contingencies, purchase or construction of fixed assets, or other uses
  • Some governing boards may delegate designation decisions to internal management. Such designations are considered to be included in board-designated net assets

• Definition indicates a need for NFPs to have policies and/or practices regarding board-designations on net assets; even if no designations

• Optional to disclose in tabular, required disclosure in footnotes
Board-designated net assets

Note 13 - Net Assets Without Donor Restrictions

The Board of Directors of XYZ Organization has several standing board policies that affect the presentation of board designations on net assets. Bequests without donor restrictions are designated for long-term investment (quasi-endowment). The quasi-endowment fund balance totaled $35,000 at December 31, 20XX. Additionally, the Board of Directors has established an operating reserve with the objective of setting funds aside to be drawn upon in the event of financial distress or an immediate liquidity need. The operating reserve balance totaled $1,300 at December 31, 20XX.
## Information About Available Resources & Liquidity

<table>
<thead>
<tr>
<th>Qualitative Disclosures</th>
<th>Quantitative Information</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategy for addressing risks that may affect liquidity</td>
<td>Include information that communicates the availability of an NFP’s financial assets at the balance sheet date to meet cash needs within one year of the balance sheet date</td>
</tr>
<tr>
<td>Policy for establishing liquidity reserves</td>
<td>Can be on the face of the Statement of financial position or in the notes</td>
</tr>
<tr>
<td>Information that communicates how NFP manages its liquid resources available to meet cash needs for general expenditures within one year of the balance sheet date</td>
<td></td>
</tr>
</tbody>
</table>
Note G

The following reflects Not-for-Profit Entity A’s financial assets, as of the balance sheet date, reduced by amounts not available for general use because of contractual or donor-imposed restrictions within one year of the balance sheet date. Amounts not available include amounts set aside for long-term investing in the quasi-endowment that could be drawn upon if the governing board approves that action. However, amounts already appropriated from either the donor-restricted endowment or quasi-endowment for general expenditure within one year of the balance sheet date have not been subtracted as unavailable.
LIQUIDITY – EXAMPLE FOOTNOTE

Financial assets, at year-end XXX,XXX

Less those unavailable for general expenditures within one year, due to

Contractual or donor-imposed restrictions

Restricted by donor with time or purpose restrictions (XX,XXX)

Subject to appropriation & satisfaction of donor restrictions (XXX,XXX)

Investments held in annuity trust (X,XXX)

Board designations

Quasi-endowment fund, primarily for long-term investing (XX,XXX)

Amounts set aside for liquidity reserve (X,XXX)

Financial assets available to meet cash needs for general expenditures within one year XX,XXX
Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use, within one year of the balance sheet date, comprise the following:

- Cash & cash equivalents: XX,XXX
- Accounts receivable: X,XXX
- Operating investments: X,XXX
- Promises to give: X,XXX
- Distributions from assets held under split-interest agreements: X,XXX
- Distributions from beneficial interests in assets held by others: X,XXX
- Endowment spending-rate distributions & appropriations: XX,XXX

XX,XXX
Can present as indirect or direct

If direct is presented, the presentation of the indirect reconciliation is no longer required
Presentation of Expenses

- Expenses have to be presented by natural classification & functional classification in one location
- Can be shown on face statements or notes
- Expenses on SOA can be shown by natural classification or functional
- Voluntary health & welfare organizations are no longer required to report a separate statement of expenses of functional expenses but would have the same flexibility as other NFPs
EXPENSES – ADDITIONAL ITEMS

- New requirement to provide qualitative disclosure about methods used to allocate expenses attributable to more than one program

- ASU refines some definitions & enhanced guidance
  - Mgmt & Gen – includes additional examples
  - Implementation guidance to help distinguish between direct conduct & direct supervision of program or supporting services
Example Footnote Disclosure for Expenses

The financial statements report certain categories of expenses that are attributable to more than one program or supporting function. Therefore, these expenses require allocation on a reasonable basis that is consistently applied. The expenses that are allocated include depreciation, interest & office & occupancy, which are allocated on a square-footage basis, as well as salaries & benefits, which are allocated on the basis of estimates of time & effort.
### EXPENSES BY NATURE & FUNCTION

#### 20X2

<table>
<thead>
<tr>
<th></th>
<th>Program Activities</th>
<th>Supporting Activities</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>A</td>
<td>B</td>
</tr>
<tr>
<td><strong>Salaries/benefits</strong></td>
<td>$</td>
<td>- $</td>
</tr>
<tr>
<td><strong>Rent/utilities</strong></td>
<td>- $</td>
<td>- $</td>
</tr>
<tr>
<td><strong>Professional fees</strong></td>
<td>- $</td>
<td>- $</td>
</tr>
<tr>
<td><strong>Supplies</strong></td>
<td>- $</td>
<td>- $</td>
</tr>
<tr>
<td><strong>Depreciation</strong></td>
<td>- $</td>
<td>- $</td>
</tr>
<tr>
<td><strong>Interest</strong></td>
<td>- $</td>
<td>- $</td>
</tr>
<tr>
<td><strong>Total expenses</strong></td>
<td>- $</td>
<td>- $</td>
</tr>
</tbody>
</table>

#### 20X2

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<td><strong>Supplies</strong></td>
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<tr>
<td><strong>Depreciation</strong></td>
<td>- $</td>
<td>- $</td>
</tr>
<tr>
<td><strong>Interest</strong></td>
<td>- $</td>
<td>- $</td>
</tr>
<tr>
<td><strong>Total expenses</strong></td>
<td>- $</td>
<td>- $</td>
</tr>
</tbody>
</table>
Presentation of Net Investment Return

- Presented net of external & direct internal investment expenses (other than those from programmatic investing)
- No longer required to disclose expenses netted against investment return
- NFP HC entities with “other than trading” securities will continue to break-out UR gains/losses below the performance indicator
Takeaways

• NFP’s need to be involved in drafting financial statements
• Early adoption?
  • Most provisions can be adopted without adopting standard, except underwater endowments, disclosure of netted investment expenses, indirect reconciliation of SOCF
• Implementation considerations
  • Training for teams
  • Changes needed for tracking net assets or reports run out of system?
  • Decisions where options are available
    • SOA presentation
    • Disaggregation on face of statements or notes
    • Functional expenses
• Board designated information
• Liquidity Disclosures – need to develop policies
Resources
Resources – Revenue Recognition

• BKD Revenue Recognition webpage –
  http://www.bkd.com/hot-topics/revenue-recognition.htm

• bkd.com Article – Revenue Recognition: A Comprehensive View for Health Care Entities

• AICPA Webpage – Revenue from Contracts with Customers
  • https://www.aicpa.org/interestareas/frc/accountingfinancialreporting/revenuere cognition.html

• AICPA Webpage – Implementation page of Revenue Recognition
  • https://www.fasb.org/cs/Satellite?c=Page&cid=1176169257359&pagemain=FASB%2FPage%2FImageBridgePage
Resources – Contributions

- BKD webinar October 16, 2018
  - https://bkd.com/search-solr?keys=ASU+2018-08%3A+Clarifying+the+Scope+and+the+Accounting+Guidance+for+Contributions+Received+and+Contributions+Made

- bkd.com Article – New NFP guidance

- AICPA article – New FASB Standard Addresses Accounting for Grants and Contracts
Resources – NFP Reporting Model

- bkd.com Article – Lessons Learned from Early Adopters

- BKD webinar – New NFP Reporting Standard
  - [https://bkd.com/thoughtware?industry[0]=4171&type[0]=8&page=2](https://bkd.com/thoughtware?industry[0]=4171&type[0]=8&page=2)

- AICPA article – New FASB Standard Addresses Accounting for Grants and Contracts
With you for the home stretch.