



Updated Multiple Element Revenue Guidance Now Widely Applicable

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In September 2009, through the issuance of Accounting Standards Update No. 2009-13 and 2009-14, the Financial Accounting Standards Board (FASB) ratified key changes to the codification. Specifically updated was the guidance about revenue arrangements with multiple deliverables and certain revenue arrangements that include software elements. The guidance is located in Subtopic 605-25, Revenue Recognition—Multiple-Element Arrangements (MeA) and Subtopic 985-605, Software Revenue Recognition of the FASB codification.

Based on the FASB's transition terms, many companies, such as early adopters and public companies issuing quarterly financial statements, have already adopted this new guidance. With the 2011 year-end financial reporting season here, it's now time for all companies that offer products within the scope of these updates to embrace and implement the new guidance.

The updated standards has led to the:

- Establishment of a hierarchy for nonsoftware transactions whereby an entity can use its best estimate to determine selling price in the absence of vendor-specific objective evidence (VSOE) or third-party evidence (TPE)
- Elimination of the residual method of allocating arrangement consideration to nonsoftware delivered elements within an arrangement
- Removal of tangible products containing both software and nonsoftware components that together deliver the products' essential functionality from the scope of software revenue recognition guidance
- Significant expansion of disclosure requirements

Organizations that have already gone through the adoption process have tested the waters with their presentation and disclosure and have come away with a handful of important takeaways.

Don't Be Caught Off Guard by the New Revenue Guidance

Take this opportunity to reexamine your revenue reporting policies and consider a formal documentation of your conclusions, even if you don't think the new guidance impacts you. In general, the scope of the new guidance affects those with multiple-element revenue arrangements or arrangements that involve software and other deliverables.

Understand Special Considerations of Certain Arrangements with Hardware and Software Elements

If you sell software that works in conjunction with related hardware, the new guidance may have a significant impact on your policies and procedures. As indicated above, the new guidance removes tangible products containing both software and nonsoftware components that together deliver the products' essential functionality from the scope of software revenue recognition guidance. While many believe this results in positive changes because of generally faster revenue recognition, the positive aspects may be accompanied by new and sometimes challenging reporting requirements.

Preparers who sell products containing both hardware and software may fall into the habit of continuing to apply software revenue recognition guidance to the software components of those arrangements. These preparers need to be particularly careful when applying interaction guidance. The new MeA guidance should be applied for separation and allocation of only those software components (and related maintenance) deemed not to deliver the product's essential functionality, such as optional software modules and upgrades. Those software elements that don't contribute to the hardware's essential functionality will continue to fall under the software revenue recognition guidance. This could result in a bifurcation of software elements included in a single transaction into two different revenue recognition guidelines.

Estimated values must be supported

The new guidance requires value to be allocated to deliverables using relative selling values. This requires that the value of each deliverable

be quantified. One of the aspects of this new guidance that has received significant attention, and one that is related to assigning values, is that it doesn't require an entity to have VSOE or TPE: If those are available they must be used, but if they aren't, you may use your own estimated selling price to assign value. For this, management must have controls and processes to support its conclusions. For example, similar deliverables should have a similar selling price when sold in similar arrangements.

Take Time to Understand the Transition Guidance and Disclosures

The update is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. So, if you're a December 31 year-end and the new guidance impacts you, you should apply the guidance for your 2011 transactions. For prior periods that are presented, the guidance gives a choice to apply retrospectively (recast prior results) or to leave as presented. Whichever decision is made for prior periods, specific disclosures are required. Keep in mind that if applying guidance to your 2011 activity has a significant impact, then *not* applying the guidance retrospectively may result in incomparable results.

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