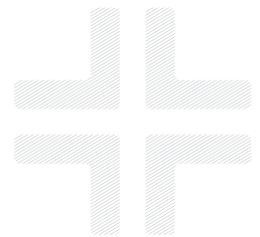




THE NEW REVENUE RECOGNITION ACCOUNTING: WHAT WILL YOUR IMPACT BE?

ASC 606 Considerations for Healthcare Organizations

The impact of ASC 606 (Revenue from Contracts with Customers) affects virtually all industries, including healthcare. The far-reaching revenue recognition framework will impact not only a company's accounting but also financial reporting, systems, processes, internal controls, financial ratios and contracts.



Implementing the new revenue recognition accounting (ASC 606) is imminent. All private entities must adopt it for fiscal years beginning after December 15, 2018 (ie. January 1, 2019 for calendar year-ends).

Use this high-level assessment tool to assess whether your ASC 606 impact will be minimal, moderate or significant, and identify areas with more complexity. User guide: consider distinct revenue streams; pay closer attention to large, customized arrangements; and bunch generic transactions and evaluate as a group.

We've **bolded** the most sensitive and complex accounting judgements for you.

STEP ONE

1 Identify the Contract

- The “contract with customer” relates to the arrangement between a healthcare provider and its patients and/or third-party insurers or government payers.
 - Special consideration should be made for arrangements where the provider is one of many participating providers in a health plan network.
- The contract must include all necessary approvals. It must identify any/all legally enforceable rights, obligations, and payment terms.
- A healthcare provider must evaluate a patient’s **intent and ability to pay** for services provided. Scenarios that may require additional judgment and analysis include:
 - Uninsured, under-insured and new patients (especially when admitted under an emergency situation).
 - Contracts with third-party government payers (e.g., Medicare), where payments to a healthcare provider may be subject to retrospective take-backs upon determination of final settlements.
- Consider generic vs. **customized agreements**. Custom arrangements will require individual analysis; generic arrangements will not.
- Agreements with **unilateral termination clauses** are not ASC 606 revenue contracts.
- Do not move to Step 2 unless an ASC 606 “contract” exists.

STEP TWO

2 Identify the performance obligations

- Begin by listing all of the services to be delivered under each patient arrangement.
- Next, consider this list from the patient’s perspective. Are all of the services the patient ultimately expects to receive on the list? Add/subtract as needed.
- Last, determine which promises are ASC 606 performance obligations:
 - A contract may entail a single performance obligation, such as a routine office visit, or multiple performance obligations, such as arrangements between extended care facilities and their residents (under which various residential and health care services are provided).
 - A promise is a separate performance obligation if it is “**distinct.**” “Distinct” is very similar to the current concept of a deliverable with standalone value to the patient. **Highly interdependent or integrated deliverables** are usually not “distinct” for ASC 606.
 - Disregard any promised services that are immaterial at the contract level.
 - Patient options for additional services (for free or at a discount)** are usually a separate performance obligation.
- This step is the **most critical part** of your assessment.
- Do not move to Step 3 until you know how many and what performance obligations there are.

STEP THREE

3 Determine the transaction price

- Approach this step at the contract level.
- Start with the fixed price stated in the contract.
- Include **good-quality estimates of probable variable consideration** (both positive and negative), such as anticipated credits to patients, refundable entrance or other fees, retrospective third-party payer adjustments, implied price concessions, charity care, etc.
- Once the fixed and variable portions of the transaction price are determined, evaluation of the **likelihood of collection** must be made. If collection is not reasonably assured, a more practical approach would be to reduce the amount of revenue recognized upfront and recognize any future cash receipts as revenue only when received.
- Do not move to Step 4 until you quantify the total transaction price.

STEP FOUR

4 Allocate the transaction price to the performance obligations

- Skip to Step 5 if there is only one performance obligation.
- Allocate Step 3's total transaction price amongst the performance obligations (from Step 2) based on **relative standalone selling prices**.
 - You may use reasonable estimates** in the allocation process if quoted prices are not available.
 - Long-term care contracts may contain multiple performance obligations given revenues are earned by providing a variety of services (home health care, assisted living, recreational and residential services, etc.), and the pattern of recognition for each service may vary.
- Variable consideration may be allocated entirely to one performance obligation if it relates specifically to it.**

STEP FIVE

5 Recognize revenue for each performance obligation

- Recognize revenue when (at a point in time) or as (over time) the patient receives the service.
- Recognize allocated revenue (from Step 4) separately as each performance obligation is satisfied.
- Consideration should be made for the methodology under which the healthcare provider is paid by third-party payers (fee-for-service, per diem, per case, episodic, etc.).
- A healthcare provider should consider the individual patient's life when determining the appropriate pattern of recognition, especially under long-term care arrangements.



AREAS WITH SPECIAL CONSIDERATIONS:

- Contract modifications
- Retrospective third-party payer adjustments and/or settlements
- Upfront or refundable contract costs
- Uninsured or under-insured patients
- Long-term care contracts
- Impact on internal controls and general ledger systems
- Expanded financial statement disclosure requirements
- Potential restatement of prior year financial statements

Our healthcare professionals have developed a readiness assessment with respect to implementation of ASC 606 for healthcare organizations, including assessment of the five-step model as it applies to your organization, tailored plans for implementation, and pro-forma financial statement footnote disclosures to assist your organization in conforming with the new guidance. Please contact a Withum professional today to begin your assessment.

The information presented in this publication is not necessarily all inclusive, does not constitute accounting, legal, tax or any other advice and should not be relied upon without first consulting with appropriate qualified professionals for your individual business facts and circumstances.



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