

This is a reminder that ASC 606, Revenue Recognition, also includes several footnote disclosure requirements. Failing to consider these disclosure requirements is resulting in peer review findings.

In the MICPA's peer review process, we are seeing numerous instances where a firm has evaluated their client's consideration of the new pronouncement, appropriately determined it to have an immaterial impact on a balance, and then stopped right there. When preparing their financial statements, they have neglected to include the new required disclosures.

ASC 606 has several qualitative and quantitative disclosure requirements. Even if the dollar amount of revenue to be recognized under the new rules is not materially different than under the prior rules, these disclosures related to its contract revenues are still required. While it is always possible that omitting these disclosures might not influence a reader, the audit standards require that evaluation to be documented in the audit workpapers – and included on the list of uncorrected misstatements, unless trivial.

So a note to the wise – every financial statement of a client with revenue from contracts with customers should include these new required footnote disclosures, even if their revenue recognition has not been materially impacted by the new rules!

Q: If I conclude that my existing footnotes include most relevant disclosures required by the standard, but not all of them, how should I document this conclusion?

A: If you use third-party disclosure checklists, you can make notations on that checklist to indicate that you considered a particular disclosure requirement and why you determined that it was not qualitatively material. In similar fashion, as mentioned above, you should record this information on your list of uncorrected misstatements. One widely used third-party practice aid for documenting uncorrected misstatements includes a section for numeric misstatements and another section for qualitative misstatements such as omitted disclosures that are considered immaterial.

Q: I have a nonprofit organization with some revenue from contracts with customers (e.g., program services); however, the balance of this revenue is not material to the financial statements. Does ASC still apply?

A: Yes, but you can use the same approach to documenting immateriality as described in the first question. In this case, the important considerations are 1) the immateriality of the contract revenue balance and 2) whether there are enough relevant disclosures to meet the overall spirit of ASC 606. When some, but not all, of the disclosure requirements are met, it is best to document which are not included and the reason.

Q: Do the disclosure requirements of ASC 606 apply to compilations with disclosures?

A: Yes. If the compilation engagement is prepared on the basis of U.S. GAAP, then all the same materiality considerations apply to these engagements.

Q: Do the disclosure requirements of ASC 606 apply to tax-basis financial statements?

A: If the tax-basis financial statements include elements comparable to U.S. GAAP basis financial statements, then comparable disclosures should be present. If the overall disclosures meet the overall

objectives of ASC 606, but some elements are missing, then document this condition along with your conclusion about their immateriality.

Q: Do I need to document uncorrected misstatements in a review engagement?

A: Since the accountant's conclusion about reviewed financial statements is whether the accountant was "aware of any material modifications that should be made to the financial statements," then consideration of the materiality of uncorrected disclosure misstatements should also be documented. As with other instances where most, but not all, of a set of disclosure requirements are met, you should document our basis for concluding that disclosure misstatements are not material.

Q: Why is all this discussion about disclosure materiality important to peer review?

A: FASB ASC §105-10-05, Overview and Background, in paragraph 6 states that the provision of the Codification need not be applied to immaterial items. While this is not a free pass to omit disclosures, with proper documentation, it can show that you were aware of requirements, considered them, and made a sound professional judgment about the materiality of disclosure misstatements.