ASC 606 Revenue Recognition

# IMPLEMENTATION ISSUES FOR HEALTHCARE ENTITIES

Accounting Standards Codification 606, *Revenue from Contracts with Customers* (ASC 606), is in effect for all companies that issue financial statements in accordance with Financial Accounting Standards Board (FASB) rules. Below, we walk through the standard's five-step revenue recognition process and highlight common implementation issues for nongovernmental healthcare entities.

## 1 Identify the contract with the customer.

- If the answer to any of the following is no, or cannot be answered, then a contract does not exist:
  - Does the patient intend to pay you?
  - Are those obligations legally enforceable?
  - Is it probable that the organization will collect all the consideration to which it is entitled?
- *Consider*: ambulance arrivals, emergency room visits and admissions, patients who refuse or are unable to sign required paperwork.
- Contract can be explicit (i.e., a written agreement) or implicit (i.e., based on customary business practices). Either way, patient must clearly have the intent and ability to pay.

## 2 Identify separate performance obligations.

- Does the contract have multiple deliverables?
- For skilled nursing facilities, each day might be a separate performance obligation, depending on circumstances.

## 3 Determine the transaction price.

- One of the most significant changes in the new standard involves variable consideration.
- Most healthcare entities accept payment that is less than standard charges, which is a form of variable consideration.
- Seller (or service provider) must now assess likelihood that variable revenue (positive and negative) will be realized.
- Use either "expected value" (probability weighted) or "most likely amount" method.
- Most healthcare entities are analyzing patient mix based on the type of payer ("portfolio approach").
- Bad debts will be reflected in operating expenses rather than in net patient revenue.

## 4 Allocate the transaction price among the performance obligations.

- Allocation is based on prices charged for goods and services when they are sold separately.
- If no standalone prices, then estimate allocation amounts using market prices, cost plus expected margin, or "residual" prices (i.e., package price minus the sum of other obligations that *do* have standalone prices).
- Consider history of offering discounts when allocating transaction prices for bundled goods and services.
- Variable consideration may be allocated to one or more — but not necessarily all — performance obligations.

## 5 Recognize revenue when (or as) the performance obligations are satisfied.

- Revenue recognized over time as performance obligations are satisfied.
- In theory, this step should not differ much from current practice.

### Next Step: Contact Your CRI Advisor

The time for action is now! CRI is ready to help you prepare for and adopt this landmark accounting standard. Contact us at **healthcare@CRIcpa.com**.