Kakimoto & Nagashima LLP
Certified Public Accountants
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NEWSLETTER

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Any Questions?

We are committed to providing our clients with quality and excellent services.

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Summary of Articles

Revenue Recognition Updates Issued

In 2016, the U.S. Financial Accounting Standards Board issued the following three updates related to ASC Topic 606, Revenue from Contracts with Customers: (a) Accounting Standards Update 2016-08, "Principal versus Agent Considerations (Reporting Revenue Gross versus Net)"; (b) Accounting Standards Update 2016-10, "Identifying Performance Obligations and Licensing"; and (c) Accounting Standards Update 2016-12, "Narrow-Scope Improvements and Practical Expedients". These new Updates clarify some aspects of ASC Topic 606, and thus, could require companies to fine tune the implementation of ASC Topic 606. Accordingly, all companies should begin to assess the impact of these new amendments.

IRS announced changes to the ITIN Program

In August 2016, the IRS released Notice 2016-48 explaining changes to the Individual Taxpayer Identification Number (ITIN) program as required by the Protecting Americans from Tax Hikes (PATH) Act signed into law in December 2015. Under the Notice, certain ITINs cannot be used on 2016 tax returns unless they are renewed. The article explains notable ITIN program changes.

Enterprise Risk Management

When you think of risk management, the first thing that comes to mind is worse-case scenarios and crisis management plans. However, this could also mean best-case scenarios, strategic plan improvement, and increased probability of achieving business objectives. Our article explains the basic concepts of enterprise risk management.

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Revenue Recognition: Accounting Standard Updates

In May 2014, the U.S. Financial Accounting Standards Board ("FASB") issued Accounting Standards Update 2014-09, "Revenue from Contracts with Customers" ("ASU 2014-09"). ASU 2014-09 creates a new ASC topic – Topic 606 – which will replace almost all existing U.S. GAAP revenue recognition guidance. In response to stakeholder feedback and implementation issues, the FASB deferred the effective date of ASU 2014-09 by one year; the International Accounting Standards Board deferred the effective date of its new revenue standard (IFRS 15) as well. In addition, the Boards' Transition Resource Group was formed to address application concerns and to assist in transition guidance to the new standard.

In 2016, FASB issued the following three updates related to ASC Topic 606, Revenue from Contracts with Customers: (a) Accounting Standards Update 2016-08, "Principal versus Agent Considerations (Reporting Revenue Gross versus Net)" ("ASU 2016-08"); (b) Accounting Standards Update 2016-10, "Identifying Performance Obligations and Licensing" ("ASU 2016-10"); and (c) Accounting Standards Update 2016-12, "Narrow-Scope Improvements and Practical Expedients" ("ASU 2016-12").

The objective of the Updates is not to change the core principle of ASC Topic 606 which is based on the five-step model below. Rather, the amendments intend to reduce (a) the potential diversity in practice at initial application, and (b) the cost and complexity of applying ASC Topic 606.

1. Identify the contract with a customer.
2. Identify the performance obligations in the contract.
3. Determine the transaction price.
4. Allocate the transaction price to the performance obligations in the contract.
5. Recognize revenue when (or as) the entity satisfies a performance obligation.

Principal versus Agent (Reporting Revenue Gross or Net) (ASU 2016-08)

The core objective of ASU 2016-08 is to decrease the potential diversity arising from inconsistent application of the principal versus agent guidance included in ASU 2014-09. Under ASU 2014-09, when another party is involved in providing goods or services to a customer, an entity is required to determine whether the nature of its promise is to provide the specified good or service itself (a principal) or to arrange for that good or service to be provided by the other party (an agent). A principal recognizes revenue on a gross basis, whereas an agent recognizes revenue on a net basis. An entity is a principal if it controls the specified good or service before that good or service is transferred to a customer. The guidance provided by ASU 2014-09 included five indicators to assist an entity in evaluating control.

ASU 2016-08 intended to improve the operability and comprehension of the implementation guidance on principal versus agent considerations by clarifying the following:

- An entity determines the nature of each specified good or service (for example, whether it is a good, a service, or a right to a good or service). Accordingly, an entity could be both a principal for some specified goods or services and an agent for others.
- If an entity controls specified goods or services before it is transferred to the customer, the entity is a principal. ASU 2016-08 clarifies that the indicators "do not override the assessment of control" and, therefore, should not be considered, in itself, determinative.
- In case an entity cannot ascertain control, the entity would use three indicators (instead of the five indicators noted in ASU 2014-09): (i) whether "the entity is primarily responsible for fulfilling the promise to provide the specified good or service"; (ii) whether "the entity has inventory risk before the specified good or service has been transferred to a customer or after transfer of control to the customer"; and (iii) whether "the entity has discretion in establishing the price for the specified good or service".

Performance Obligations (ASU 2016-10)

In ASU 2016-10, the FASB clarified matters related to performance obligation identifications; it also changed guidance related to IP licenses.

In Step 2 of the revenue recognition model, an entity is required to identify its performance obligations in a contract with a customer. ASU 2016-10 updates guidance in the following areas:

- Before an entity can identify its performance obligations, the entity first identifies the promised goods or services in the contract. ASU 2016-10 allows the entity not to assess whether promised goods or services are performance obligations if they are immaterial in the context of the contract with the customer.
- To identify performance obligations in a contract, an entity evaluates whether promised goods and services are distinct by using two criteria, one of which is that the promises are separately identifiable. ASU 2016-10 improved the guidance on assessing that criterion by better articulating the principle and by revising the related factors and examples.

Narrow-Scope Improvements and Practical Expedients (ASU 2016-12)

ASU 2016-12 amends the following areas:

- Assessing the collectability criterion and accounting for contracts that do not meet the criteria for Step 1
- Presentation of sales taxes and other similar taxes collected from customers
- Noncash consideration
- Contract modifications at transition
- Completed contracts at transition
- Technical correction

Effective Dates of the ASUs

The effective dates for ASU 2016-08, ASU 2016-10, and ASU 2016-12 are the same as the effective dates for ASU 2014-09 which are as follows:

Public Entities

Public entities are required to apply the ASUs for annual reporting periods beginning after December 15, 2017, including interim reporting periods therein.

Nonpublic Entities

Nonpublic entities are required to adopt the ASUs for annual reporting periods beginning after December 15, 2018, and interim periods within annual reporting periods beginning after December 15, 2019.

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IRS Released Notice 2016-48 to Address Changes to the ITIN Program

On August 4, 2016, the IRS released Notice 2016-48, which contains changes to the Individual Taxpayer Identification Number (ITIN) program as required by the Protecting Americans from Tax Hikes (PATH) Act of 2015 signed into law in December 2015.

Background
An ITIN is a nine-digit tax processing number issued by the IRS that is formatted like a Social Security Number (SSN), XXX-XX-XXXX. The IRS issues ITINs to individuals who are required to have a U.S. taxpayer identification number for U.S. tax purposes but who are not eligible to obtain an SSN from the Social Security Administration.

Under the PATH Act, certain ITINs issued in the past will not be valid for use on a tax return unless renewed.

1. Unused ITINs – If an ITIN has not been used on a federal tax return at least once in the last three years (2013, 2014, or 2015), it will no longer be valid to use on a tax return as of January 1, 2017.
2. Expiring ITINs – ITINs issued prior to 2013 (even those that have been used on a tax return in the last three consecutive years) are set to expire based on a multi-year schedule. The first ITINs that will expire under the schedule are those with the fourth and fifth (middle digits) of 78 or 79 (Example 9xx-78-xxxx). These ITINs will no longer be effective beginning January 1, 2017. Individuals whose ITINs contain middle digits of 78 or 79 should be receiving a letter from the IRS notifying them of the upcoming expiration.

Failure to renew an expired ITIN before filing one's 2016 tax return could result in refund delays and ineligibility for certain tax credits, such as the Child Tax Credit and the American Opportunity Tax Credit until the ITIN is renewed. However, an ITIN holder who does not need to file a tax return next year does not need to take any action.

Also, for those ITINs used only on informational returns filed or furnished by third parties, such as Form 1099 or Form 1042-S, a taxpayer is not required to renew the ITIN, and the ITIN may continue to be used for informational return purposes regardless of whether it has expired for individual income tax return filing purposes.

Renewal Process
A taxpayer may renew an unused or expiring ITIN beginning October 1, 2016 by completing the newest version of Form W-7, Application for IRS Individual Taxpayer Identification Number, which was released in September 2016. For renewal purposes, a taxpayer is not required to attach a tax return when submitting a Form W-7 (check the box that says "renewal") but he or she must include all of the information and documentation required by the instructions including an original certified passport to establish their identity, foreign status and U.S. residency status. The W-7 renewal package may be submitted by mail, sent via a certified Acceptance Agent, or submitted through an appointment with the IRS Taxpayer Assistance Center. Once the ITIN is renewed, the individual can continue to use the same ITIN which will remain in effect unless it is not used on a tax return for three consecutive years.

Additionally, an individual taxpayer with an ITIN middle digit of 78 or 79 may renew the ITIN with his/her spouse as well as any dependents claimed on the tax return at the same time instead of renewing each member's ITIN separately over several years.

Beginning October 1, 2016, the IRS will not accept passports that do not include a date of entry into the U.S. as stand-alone identification for dependents from countries other than Canada or Mexico or dependents of military members overseas. In such cases, applicants must submit, in addition to the passport the following: (1) U.S. medical records for dependents under age six or U.S. school records for dependents under age 18, or (2) a rental of bank statement or a utility bill listing the applicant's name and U.S. address for dependents aged 18 and above.

IRS

ITINs with middle digits other than 78 or 79 that have been used within the last three consecutive tax years should not be renewed and require no immediate attention from the ITIN holder.

Please contact us if you have any questions or need assistant renewing your ITIN.♦

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We're Here to Help
Please contact us if you have additional questions or would like further information on how the new ASUs may impact your company.♦

Enterprise Risk Management

"The biggest risk is not taking any risk. In a world that is changing really quickly, the only strategy that is guaranteed to fail is not taking risks."
-Mark Zuckerberg

What is Enterprise Risk Management (ERM)? According to COSO, ERM is defined as a process, effected by an entity's board of directors, management and other personnel, applied in strategy setting across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives.

The definition reflects certain fundamental concepts. Enterprise risk management is:

- A process, ongoing and flowing throughout the entity
- Effected by people at every level of an organization
- Applied in strategy setting
- Applied across the enterprise, at every level and unit, and includes taking an entity-level portfolio view of risk
- Designed to identify potential events that, if they occur, will affect the entity and to manage risk within its risk appetite
- Able to provide reasonable assurance to an entity's management and board of directors
- Geared to achievement of objectives in one or more separate but overlapping categories

Risk management is not about avoiding the risk but rather understanding and managing the risk. Risk includes the potential for failure that could result in loss, harm or missed opportunity-the risk of inaction. Total avoidance of risk will lead to competitive disadvantage while taking too much risk will lead to destruction.

It is the responsibility of management to assess the risk and determine the possible or probable impact of the events. Risk management is basically how you respond to a situation or challenges from both inside or outside sources that could have a possible effect on the enterprise.

Implementation of risk management should be part of the strategy-setting process activity. A risk should be evaluated relative to alternative strategies and considered when deciding on appropriate courses of action. ERM should be able to provide an action plan to mitigate the impact of undesirable events and improve chances of success.

ERM eight implementation steps:

- Identify the risk by surveying people across the organization.
- Quantify exposure by determining the likelihood of occurrence and the potential impact of events.
- Assess the current status by considering what steps have been taken relative to determine existing exposure.
- Assign responsibility for oversight of action plans for each risk.
- Establish a review process by top management and the board of directors.
- Prioritize risk exposure in terms of the greatest potential threats and their impact.
- Assess potential mitigation strategies for potential action steps relative to each risk exposure on a priority basis.
- Evaluate the potential of identified opportunities relative to each risk in terms of how the organization could utilize the situation to achieve an advantage.

Generally, good governance is to be able to manage challenges, minimize uncertainty and prepare for inevitable crisis or take advantage of unexpected opportunity. Although historical data can provide valuable lessons on how to manage risk, it will not give you a perfect plan to handle it. The important factors in managing risk are the leadership and governance of an enterprise because critical risks need to be addressed by upper management. Upper management plays an important role in managing enterprise risk since they are in the position that have the firsthand knowledge of potential risks facing the organization and have the experience and skills to deal with the results. They are also responsible in monitoring the strategic plan and evaluate which risks have the potential to impact the enterprise.

Although management plays a very important role, ultimately, everyone in the enterprise has the responsibility to perform, because decisions related to risk are made daily at every level of enterprise. It is important that all personnel within the enterprise share the same understanding of key decision-making skills, processes, and tools.

An effective ERM strategy attempts to achieve an acceptable balance between growth, risk, and returns. It should be linked to the enterprise appetite for risk. Based on the appetite for risk, the enterprise can develop an effective alignment of people, processes, infrastructure, and how to allocate resources. Obviously, every organization is unique when it comes to risk appetite. A certain enterprise may be assertive in its strategy and risk appetite, while another may be more conservative. The strategy that should be implemented should match with the culture of the enterprise. Culture may be harder to change than strategy, so it is important to ensure that they are aligned.

In order to maintain a successful business, risk must be taken to take advantage of opportunities and they must be managed instead of avoiding it. Being prepared and forward looking are keys to survival and success.♦