Consumer Products & Trade Spend Accounting

Types of Trade Spend

► Trade promotion or spending comes in a variety of forms including:

- Discounts
- Cooperative advertising
- Point-of-purchase (POP) displays
- Rebate programs
- Coupons
- Contests and sweepstakes
- Gifts and premium money
- In-store tasting and sampling
- Slotting fees

Current Recognition

- Recognize the cost of the incentive at the later of:
  - the date at which the related revenue is recognized by the vendor
  - the date at which the sales incentive is offered (i.e. the incentive is offered after the vendor has recognized revenue), for example, coupons for discounts issued on products already sold to retailers

- Rebates or refunds of a specified amount redeemable by the customer based on volumes purchased or for remaining a customer for a specified time period are recognized based on a systematic allocation of the cost of providing the rebates as earned by the customer

Income Statement Presentation

- Recognize as an adjustment to the selling price of vendor's product (reduction of revenue)
  - Cash payments, credits, or equity instruments that a customer can apply against trade amounts owed to a vendor
  - Slotting fees and similar product development or placement fees
  - Buydown programs to reimburse, compensate or issue credit memos to a retailer for the retailer's decreased revenue per unit during a specified promotion period

Income Statement Presentation, continued

- Recognize as a cost incurred by the vendor for assets or services received from the customer (cost or expense) if both conditions are met:
  - the vendor receives an identifiable benefit (goods or services) in exchange for the incentive that is sufficiently separable from the customer's purchase of products such that the vendor could have entered into an exchange transaction with a party other than the purchaser of its products in order to receive that benefit
  - the vendor can reasonably estimate the fair value of the benefit
- A free product or service offered by the vendor
- Cooperative advertising

Accounting treatment - Example

	Actuals from Year 1			Redemptions
	Gross		%	from Year 1
	Product Sales	Redemptions	of GPS	During Year 2
January	$ 1,650,000	$ 100,000	6.1%	$ 150,000
February	1,750,000	153,000	6.1%	65,000
March	2,060,000	121,000	8.7%	55,000
April	2,660,000	266,000	5.9%	36,000
May	3,380,000	348,000	10.0%	25,000
June	3,020,000	829,000	10.3%	16,000
July	2,040,000	616,000	27.5%	13,000
August	2,070,000	376,000	18.2%	6,000
September	1,360,000	344,000	25.3%	5,000
October	1,400,000	108,000	7.7%	4,000
November	1,040,000	223,000	21.4%	4,000
December	1,290,000	191,000	14.8%	1,000
Total	$ 23,720,000	$ 3,675,000	15.5%	$ 380,000
Look Back Test:				
Nov./Dec Sales	2,330,000			
Avg. Rate	15.5%			
Accrual	360,993			
Actual Usage	380,000			
Difference	(19,007)			
% Difference	-5%			

Accounting treatment - Example

	Actuals from Year 1						Redemptions from Year 1
	Gross Product Sales	Redemptions	% of GPS	Accrual Calculation			During Year 2
				Sales X Rate	Waterfall	Accrual	
January	$ 1,650,000	$ 100,000	6.1%	$ 255,639	0.00%	$ -	$ 150,000
February	1,750,000	153,000	6.1%	$ 271,132	0.00%	$ -	65,000
March	2,060,000	121,000	8.7%	$ 319,161	0.50%	$ 1,596	55,000
April	2,660,000	266,000	5.9%	$ 412,121	1.00%	$ 4,121	36,000
May	3,380,000	348,000	10.0%	$ 523,672	1.00%	$ 5,237	25,000
June	3,020,000	829,000	10.3%	$ 467,896	1.00%	$ 4,679	16,000
July	2,040,000	616,000	27.5%	$ 316,062	5.00%	$ 15,803	13,000
August	2,070,000	376,000	18.2%	$ 320,710	5.00%	$ 16,036	6,000
September	1,360,000	344,000	25.3%	$ 210,708	15.00%	$ 31,606	5,000
October	1,400,000	108,000	7.7%	$ 216,906	20.00%	$ 43,381	4,000
November	1,040,000	223,000	21.4%	$ 161,130	50.00%	$ 80,565	4,000
December	1,290,000	191,000	14.8%	$ 199,863	90.00%	$ 179,877	1,000
Total	$ 23,720,000	$ 3,675,000	15.5%			$ 382,900	$ 380,000
						Difference	$ 2,900

Accounting treatment - Example

Month	Actuals from Year 1 Gross Product Sales	Actuals from Year 1 Redemptions		Redemptions from Year 1 During Year 2
January	$ 1,650,000	$ 100,000		$ 300,000
February	1,750,000	153,000		50,000
March	2,060,000	121,000		25,000
April	2,660,000	266,000		5,000
May	3,380,000	348,000		1,000
June	3,020,000	829,000		-
July	2,040,000	616,000		-
August	2,070,000	376,000		-
September	1,360,000	344,000		-
October	1,400,000	108,000		-
November	1,040,000	223,000		-
December	1,290,000	191,000		-
Total	$ 23,720,000	$ 3,675,000		$ 381,000
% of GPS	15.5% a			
4th QTR Sales:	b	a x b	Waterfall	Accrual
October	1,400,000	216,906	40%	86,762
November	1,040,000	161,130	65%	104,734
December	1,290,000	199,863	95%	189,870
Total	3,730,000			381,366
Difference				(366)

Implementation of ASC 606, *Revenue from Contracts with Customers*

- Effective for calendar year ends
  - Public companies in 2018
  - Non-public companies in 2019
- ML&R CPE on Thursday, September 20, 2018 with Wayne Kerr, Thomson Reuters
- ML&R is offering consulting engagements throughout 2018 and 2019 to assist clients with the implementation of the new rev rec standards

Revenue Recognition: The 5 Steps

1	Identify the contract with the customer
2	Identify the performance obligations in the contract (*consider material rights*)
3	Determine the transaction price (*consider variable consideration*)
4	Allocate the transaction price to separate performance obligations
5	Recognize revenue when (or as) each performance obligation is satisfied

Revenue Recognition Under the New Standard

- Generally, incentives previously determined to be contra-revenue or expense will have the same treatment under the new model

- First quarter 2018 10Qs aren't showing significant restatements for implementation on consumer product companies

- Previously, revenue was recognized when significant risks and rewards of ownership transferred to the customer (generally, based on shipping terms). New standard requires that additional factors be considered to determine when control transfers.

- Differences could arise when entities give customers the option to acquire additional goods at a discount or free of charge (i.e. discount vouchers, gift cards issued in conjunction with purchases, loyalty or reward programs)

Determination of When a Performance Obligation is Met and Revenue Recognition

- Previously, shipping terms determined revenue recognition. New standard is based on transfer of control.
- Control = ability to direct the use of and obtain substantially all of the remaining benefits from the asset
- Benefits include:
    - using the asset to produce goods or services, to enhance the value of other assets, to settle liabilities or reduce expenses
    - selling the asset
    - pledging the asset to secure a loan
    - holding the asset

Indicators of the Transfer of Control Include

- Entity has a right to payment / customer is obliged to pay
- Customer has legal title to the asset
- Entity has transferred physical possession of the asset
  - *This has been debated as it could be interpreted as delaying revenue recognition until the customer receives the product preventing rev rec upon shipment regardless of shipping terms.*
- Customer has significant risks and rewards of ownership
- Customer has accepted the asset
  - Not relevant if customer acceptance is a formality
  - If product is delivered for trial or evaluation purposes and no payment is required by the customer until the trial period lapses, control has not transferred

Volume Discount Guidance

- Volume related rebates or price step-downs - provide customers with an option to acquire additional goods for free or at a discount
  - if volume discount results in retrospective price adjustment = variable consideration
  - if volume discount results in prospective volume discount = potential material right

Price Discount Guidance

- Price step-downs - provide customers with price decreases in future years regardless of volume of units purchased in prior years
    - if the lower price in future years is an incremental discount that the customer wouldn't have received without previously entering into the contract in the prior year = generally, a material right
    - if the decreased price is due to expected increased efficiencies in the company's processes and the price truly reflects that stand-alone selling price = generally, not a material right

Possible Changes for Volume and Price Discount Options

- If the option provides a material right to the customer, the entity will be required to allocate a portion of the transaction price to the material right at contract inception.

- The revenue allocated to the material right will not be recognized until the option is exercised or as the option is exercised (and the goods are transferred) or when the option expires. This would result in delayed revenue recognition.

- If the option does not provide a material right (option reflects the standalone selling price a customer without an existing relationship with the entity would pay), this is a marketing offer and there is no accounting until subsequent purchases occur.

Rights of Return Guidance

- Rights of return are determined consistently with prior guidance (estimate return liability and record as contra-revenue)

- Recognize:
  - Revenue for transferred products
  - Contract refund liability for refunds and credits to customers for goods expected to be returned re-measured at each reporting date with an adjustment to revenue
  - Contract asset for the right to re-sell returned goods less any additional costs to get them ready for re-sell with an adjustment to COGS - NEW

Challenges Estimating the Trade Spend Accrual

- Identifying the best and most cost effective system for tracking the incentives offered (i.e. Excel or specific software)

- Implementing internal controls to ensure that
  - proper levels of authority are in place to set limits on sales incentives offered by the Sales team
  - Accounting receives complete information from various departments timely in order to accurately estimate the liability
  - off-invoice netting items taken by customers are reconciled to previously offered and approved sales incentives

Thank You

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