Revenue: Real estate

Q&As

US GAAP

August 2024

frv.kpmg.us

Contents

Foreword 1

About this publication 2

Executive summary 3

A. Scope 7

B. Step 1: Identify the contract 27

C. Step 2: Identify the performance obligations 31

D. Step 3: Determine the transaction price 41

E. Step 4: Allocate the transaction price 52

F. Step 5: Recognize revenue 58

G. Other implementation matters 91

KPMG Financial Reporting View 108

Acknowledgments 110

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

New year, new challenges

The ongoing application of the revenue and other income standards continues to present challenges as real estate companies react to the business practices and economic environment in recent years.

Although the challenges to real estate companies have varied widely depending on the nature of their businesses and how they interact with their customers and buyers, most have experienced changes in a number of their estimates and their processes and considerations for evaluating their buyers' credit and nonperformance risk.

KPMG Handbook, Revenue recognition, illustrates how the revenue standard applies to common transactions, provides examples about common scenarios and explains our thinking on the questions that continue to arise.

This publication provides supplemental technical guidance on key issues for real estate companies, including their interaction with the leases standard. We address some of the common questions about the effects of the standards on sales of real estate and other non-lease revenue, and we hope it will advance the dialogue on these and other issues.

We will continue to provide the latest thinking that affects real estate companies.

Angie Storm and Mike Breen
Department of Professional Practice, KPMG LLP

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

About this publication

Purpose

The purpose of this publication is to assist you in understanding the requirements of Topic 606, *Revenue from Contracts with Customers* and Subtopic 610-20, *Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets*, as they apply to real estate transactions.

This publication is intended for use by preparers and other interested parties with a working knowledge of legacy real estate sales guidance, and an understanding of the revenue recognition and other income models.

Organization of the text

The publication is in Q&A format and is organized into chapters that largely reflect the steps in the revenue recognition model. Our commentary refers to the FASB Accounting Standards Codification®, when excerpts are not included, where applicable. For example, 606-10-25-1 is paragraph 25-1 of Subtopic 606-10.

We include examples to explain key concepts, and we explain the changes from legacy US GAAP. The questions and answers that have been added or substantially expanded in this edition are highlighted in the Appendix.

Terminology

Unless otherwise indicated explicitly or by comparison, we use the terms 'customer' and 'buyer' interchangeably to refer to the purchaser in a transaction involving the sale of real estate. This is because the guidance in this publication addresses both the requirements of Topic 606 on revenue recognition from sales to customers, and the requirements of Subtopic 610-20 on recognition of gains and losses from the derecognition of nonfinancial assets in transactions with parties other than customers.

We use the terms 'gain' and 'gain or loss' interchangeably to refer to the income statement effect from derecognition of nonfinancial assets in the scope of Subtopic 610-20 as the transaction may result in either and is reported in other income.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Executive summary

Scope

The guidance applies to all contracts with customers unless the customer contract is specifically in the scope of other guidance – e.g. Topic 460 (guarantees).

Topic 606 applies to contracts to deliver goods or services to a customer. A 'customer' is a party that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration.

Topic 606 is applied to part of a contract when only some elements are in the scope of other guidance.

Read more: chapter A

Step 1: Identify the contract

Contracts can be written, oral or implied by an entity's customary business practices, but must be enforceable by law.

This may require legal analysis on a jurisdictional level to determine when a contract exists and the terms of that contract's enforceability.

A contract with a customer is accounted for under the revenue model when the contract is legally enforceable, and all of the following criteria are met:

- the contract has commercial substance;
- rights to goods or services can be identified;
- payment terms can be identified;
- the consideration the entity expects to be entitled to is probable of collection; and
- the contract is approved and the parties are committed to their obligations.

If the criteria are not met, any consideration received from the customer is generally recognized as a deposit (liability).

Read more: chapter B

Step 2: Identify the performance obligations

Performance obligations do not have to be legally enforceable; they exist if the customer has a reasonable expectation that the good or service will be provided.

Performance obligations are the unit of account under Topic 606 and generally represent the distinct goods or services that are promised to the customer.

Promises to the customer are separated into performance obligations and are accounted for separately if they are both (1) capable of being distinct and (2) distinct in the context of the contract.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

A promise can be implied by customary business practices, policies or statements.

If the distinct goods or services are substantially the same and have the same pattern of transfer to the customer over time, they are combined into a single performance obligation (a 'series').

Read more: chapter C

Step 3: Determine the transaction price

Estimating variable consideration is a significant judgment for many entities.

When determining the transaction price, an entity uses the legally enforceable contract term. It does not take into consideration the possibility of a contract being cancelled, renewed or modified.

The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer, excluding amounts collected on behalf of third parties – e.g. some sales taxes. This consideration can include fixed and variable amounts.

The transaction price determination also considers:

- **Variable consideration**, which is estimated at contract inception and is updated at each reporting date for any changes in circumstances. The amount of estimated variable consideration included in the transaction price is the amount for which it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty is resolved.
- **Noncash consideration** received from a customer, which is measured at fair value at contract inception.
- **Consideration payable to a customer**, which represents a reduction of the transaction price unless it is a payment for distinct goods or services the entity receives from the customer.
- **Significant financing component**, which may exist in a contract when payment is received significantly before or after the transfer of goods or services. This could result in an adjustment to the transaction price to impute interest income/expense.

Read more: chapter D

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Step 4: Allocate the transaction price

A contractually stated price or list price is not presumed to be the stand-alone selling price of that good or service.

The transaction price is allocated at contract inception to each performance obligation to depict the amount of consideration to which an entity expects to be entitled in exchange for transferring the promised goods or services to the customer.

An entity generally allocates the transaction price to each performance obligation in proportion to its stand-alone selling price. However, when specified criteria are met, a discount or variable consideration is allocated to one or more, but not all, performance obligations.

The stand-alone selling price is the price at which an entity would sell a promised good or service separately to a customer. Observable stand-alone prices are used when they are available. If not available, an entity is required to estimate the price using other techniques that maximize the use of observable inputs – even if the entity never sells the promised good or service separately.

Read more: chapter E

Step 5: Recognize revenue

An entity first determines whether a performance obligation meets the criteria to recognize revenue over time.

If none of the over-time criteria are met, revenue for the performance obligation is recognized at the point in time that the customer obtains control of the goods or services.

An entity recognizes revenue when it satisfies its obligation by transferring control of the good or service to the customer.

A performance obligation is satisfied over time if one of the following criteria are met:

- the customer simultaneously receives and consumes the benefits as the entity performs;
- the entity's performance creates or enhances an asset that the customer controls as the asset is created or enhanced; or
- the entity's performance does not create an asset with an alternative use to the entity, and the entity has an enforceable right to payment for performance completed to date.

If control transfers **over time**, an entity selects a method to measure progress that is consistent with the objective of depicting its performance.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Control is the ability to direct the use of, and obtain substantially all of the remaining benefits from, the goods or services – or prevent others from doing so.

If control transfers at a **point in time**, the following are some indicators that an entity considers to determine when the customer obtained control. The customer has:

- a present obligation to pay;
- physical possession;
- legal title;
- the risks and rewards of ownership; and
- accepted the asset.

Read more: chapter F

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

A. Scope

Questions and Example

Q&A A10 How do you determine whether real estate sales are in the scope of Topic 606 or Subtopic 610-20?

Q&A A20 What else is in the scope of Subtopic 610-20?

Q&A A21 Does Subtopic 610-20 apply to the transfer of an option to purchase real estate?

Q&A A25 What guidance should a seller apply when it sells a noncontrolling interest in an entity that is not a subsidiary (e.g. equity method investee)?

Q&A A26 Are sales of undivided interests to noncustomers in the scope of Subtopic 610-20? What if the buyer is a customer?

Q&A A30 How does an entity apply the revenue (or other income) recognition guidance when it sells property improvements (or integral equipment) and leases the underlying land to a customer?

Q&A A40 How do guarantees affect the accounting for an accompanying sale of real estate?

Q&A A50 How do support obligations affect the accounting for an accompanying sale of real estate?

Example A50.1: Property sale with support obligation

Q&A A60 Under Topic 606, what is the unit of account for sales of condominium units within a condominium project (or similar structure)?

Q&A A70 Is a property or asset manager's carried interest (or promote) in the scope of Topic 606?

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question A10

How do you determine whether real estate sales are in the scope of Topic 606 or Subtopic 610-20?

Interpretive response: Determining which guidance applies depends on whether the buyer is a customer. If the buyer is a customer, the seller accounts for the sale under Topic 606 and recognizes revenue and cost of sales. The Master Glossary to the Codification defines a customer as "a party that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration." [Master Glossary, 360-10-40-3A]

A real estate developer predominantly in the business of selling retail land or residential units would be an example of an entity that likely is selling real estate as an output of its ordinary activities.

In contrast, a real estate investment trust (REIT) that primarily leases real estate generally would not sell real estate as an output of its ordinary activities. While some REITs often sell properties as part of their overall investment strategy, they identify the output of their normal activities as the service they provide to their tenants. This conclusion is consistent with how a REIT's operations are characterized for US federal income tax purposes.

While a REIT's income generally is tax-free (assuming it meets qualification criteria), gains on dispositions of property held primarily for sale to customers in the ordinary course of business are considered "prohibited transactions" and are subject to 100% tax. To preserve the maximum tax advantage to the REIT and its investors, a REIT generally does not sell property to customers in its ordinary course of business.

Accounting for sales to customers – Topic 606

A seller accounts for customer sales under Topic 606 and recognizes revenue and cost of sales in its income statement. The seller follows this accounting regardless of whether it sells its direct interest in the real estate or its controlling ownership interest in an entity that holds the real estate.

When a contract exists and the seller transfers control of the property, the seller derecognizes the real estate and recognizes the transaction price as revenue.

If a contract does not exist, the seller recognizes the cash received as a deposit liability, continues to report the real estate in its financial statements, depreciates it (if not held for sale), and evaluates it for impairment as necessary. [360-10-35, 360-10-40-3C, 45-9 – 45-10]

This reporting continues until a contract does exist and control of the property transfers, or until the seller meets one of these conditions:

a. the seller has no remaining obligations to transfer goods or services to the customer and all, or substantially all, of the promised consideration has been received and is nonrefundable;
b. the contract has been terminated and the consideration received is nonrefundable; or
c. the seller has transferred control of the goods or services to which the consideration that has been received relates, has stopped transferring

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

goods and services to the customer (if applicable) and has no obligation under the contract to transfer additional goods or services, and the consideration received from the buyer is nonrefundable. [606-10-25-7 – 25-8]

Accounting for sales to noncustomers – Subtopic 610-20

If the seller determines that the buyer is not a customer, it generally accounts for the sale under Subtopic 610-20 because a real estate asset is a nonfinancial asset and typically is not a business.[1] The seller recognizes a gain or loss in the income statement for noncustomer sales.

If the seller is transferring a group of assets or a controlling financial interest in a subsidiary, other considerations apply. If substantially all of the fair value of the assets of the group or subsidiary is concentrated in nonfinancial assets (e.g. real estate and intangibles) and the group or subsidiary is not a business, the seller applies Subtopic 610-20 to the sale of each distinct asset within the group or subsidiary. This includes assets in the group or subsidiary that would be financial assets if they were sold separately. These financial assets within the group or subsidiary are referred to as ´in-substance nonfinancial assets'. See Question A20. [610-20-15-4, 360-10-40-3A]

To address real estate sales to noncustomers, Subtopic 610-20 incorporates Topic 606's principles that address sales to customers. Specifically, a seller of a nonfinancial (or an in-substance nonfinancial) asset to a noncustomer applies Topic 606's guidance to determine:

a. whether a contract exists; [610-20-25-5, 606-10-25-1 – 25-8]
b. how to separate and measure one or more parts of a contract that are within the scope of other Topics; [610-20-15-9, 606-10-15-4]
c. the number of distinct assets in the disposal group; [610-20-25-6, 606-10-25-19 – 25-22]
d. the transaction price, including estimating variable consideration, constraining that consideration, and evaluating whether there is a significant financing component, noncash consideration and consideration payable to the customer; [610-20-32-3, 606-10-32-2 – 32-27, 32-42 – 32-45]
e. how to allocate the consideration in the contract to distinct assets in the disposal group; and [610-20-32-6, 606-10-32-28 – 32-41]
f. when an entity satisfies a performance obligation by transferring control of an asset. [610-20-25-6, 606-10-25-30]

Under Subtopic 610-20, when a contract exists and the seller has transferred control of the property (which includes concluding that it no longer has a controlling financial interest under Topic 810 (consolidation) if the asset is owned by a separate legal entity – see Question F90), the seller derecognizes the real estate and recognizes a gain or loss equal to the difference between the amount of consideration transferred and the carrying amount of the asset. The amount of consideration that is included in the calculation of the gain or loss includes both the transaction price determined under Topic 606 and the carrying amount of liabilities assumed or relieved by the buyer. [610-20-32-2]

If the seller is transferring a group of assets or a controlling financial interest in a subsidiary, the sale of each distinct asset within the group or subsidiary is

---

[1] For more information on the definition of a business, see KPMG Handbook, Business combinations.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

accounted for as a separate unit of account under Subtopic 610-20 as previously discussed. The seller may need to allocate the consideration to each distinct asset – e.g. if the seller does not transfer control of all of the distinct assets at the same time. [610-20-25-6, 32-2]

Similar to Topic 606, if a contract does not exist, the seller recognizes the cash received as a deposit liability, continues to report the real estate in its financial statements, depreciates it (if not held for sale), and evaluates it for impairment as necessary. [360-10-35, 360-10-40-3C, 45-9 – 45-10]

This reporting continues until a contract does exist and control of the property transfers, or until the seller meets one of the conditions in paragraph 606-10-25-7. At that time, the property and related deposit liability are derecognized and the gain or loss is recognized. [606-10-25-1 – 25-8]

Question A20

What else is in the scope of Subtopic 610-20?

Interpretive response: As discussed in Question A10, the guidance on derecognition of nonfinancial assets to noncustomers in Subtopic 610-20 applies to sales to noncustomers of nonfinancial assets and in-substance nonfinancial assets. It also applies to other transfers of these assets including sales of ownership interests in certain subsidiaries that are not businesses (see discussion on partial sales below) and other changes in circumstances that result in loss of control over the nonfinancial (or in-substance nonfinancial) assets – e.g. because of the expiration or termination of a contractual agreement, a dilution event, a government action or default of a subsidiary's nonrecourse debt (see Question F50). An entity also could lose control over nonfinancial assets and in-substance nonfinancial assets by contributing those assets to a joint venture or another noncontrolled investee (see discussion on partial sales below). [610-20-05-2]

What is a 'nonfinancial asset'?

Nonfinancial assets include land, buildings, intangible assets and materials and supplies. A nonfinancial asset does not meet the definition of either a business or a financial asset (e.g. cash, receivables, equity method investment). Nonfinancial assets may be either recognized or unrecognized (e.g. a zero carrying amount). [610-20-15-2]

Nonfinancial assets may also include properties with real estate components, like land plus property improvements and integral equipment – i.e. those properties that have been identified as in-substance real estate historically. However, just because a property was in-substance real estate under legacy US GAAP does not mean that a sale of that property is in the scope of Subtopic 610-20. The current guidance requires an entity to apply Topic 810 to sales of all businesses, regardless of whether they were in-substance real estate under legacy US GAAP. The FASB retained the legacy guidance on identifying in-substance real estate only to identify the scope of (a) sale-leaseback transactions that remain subject to the guidance in

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Subtopic 360-20 until the new leases standard is adopted[2] and (b) the non-revenue-related guidance specific to timeshare transactions within the scope of Topic 978 (time-sharing activities). The definition is no longer relevant for identifying what guidance to apply to derecognition transactions other than sale-leasebacks. [610-20-15-4, 360-20-15-2, 978-10-15-7 – 15-12]

What is an 'in-substance nonfinancial asset'?

As previously mentioned, in-substance nonfinancial assets are financial assets that are being sold either as part of a group or within a subsidiary that is not a business and for which substantially all of the fair value of the assets of that group or subsidiary is concentrated in nonfinancial assets – e.g. real estate and intangibles. When determining the fair value of the assets of the group or subsidiary, a seller should include recognized and unrecognized assets, but exclude cash and cash equivalents. The seller should also exclude liabilities that are assumed or relieved by the buyer. [610-20-15-7]

The FASB decided to use the term **substantially all** because it is commonly used throughout US GAAP. However, it did not specify a quantitative threshold for what substantially all means when applying the scope of Subtopic 610-20. In other US GAAP, substantially all generally is interpreted to mean approximately 90% or greater; however, for evaluating the scope of Subtopic 610-20, we believe that substantially all is not necessarily meant to be a bright-line quantitative threshold. When there is uncertainty about whether the 'substantially all' threshold is met (e.g. because the ratio is close to the quantitative threshold or the valuation of assets is based on unobservable (Level 3) fair value measurement inputs subject to significant measurement uncertainty), we believe qualitative factors may also be considered. The purpose of a qualitative assessment is to evaluate whether the substance of the transaction is a transfer of nonfinancial assets. We believe relevant factors to consider include but are not limited to whether the financial assets in the transaction:

- are simply a product of the property's operations – e.g. rent receivables. If so, it may be appropriate to conclude that substantially all of the fair value of the assets is concentrated in nonfinancial assets even if their fair value is at or slightly below 90% of the fair value of the set.
- lack commercial substance. If so, a quantitative assessment that includes those assets would not be appropriate. For example, if the seller arbitrarily included financial assets in the transaction that otherwise would not have been part of the set to avoid applying Subtopic 610-20, those financial assets would be excluded from the quantitative analysis. These situations can be highly judgmental and based on facts and circumstances.

When substantially all of the fair value of the group's or subsidiary's assets is concentrated in nonfinancial assets and the group or subsidiary is not a business, a seller applies Subtopic 610-20 to the sale of each distinct asset within the group or subsidiary. This includes assets in the group or subsidiary that would be financial assets if they were sold separately. [610-20-15-5]

---

[2] Sale-leaseback transactions remain subject to Subtopic 360-20 only until a company adopts ASU 2016-02, Leases (Topic 842). Topic 842 supersedes Subtopic 360-20 and provides a single accounting model for sale-leaseback transactions that applies regardless of the nature of the asset transferred.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

In some cases, substantially all of the fair value of a group's assets is not concentrated in nonfinancial assets, but the group includes a subsidiary in which substantially all of the fair value of the subsidiary's assets is concentrated in nonfinancial assets. For example, Entity A has two consolidated subsidiaries (Sub A and Sub B) and has entered into a contract with Entity D to transfer 100% of the ownership in these two subsidiaries that are not businesses. Sub A's only asset is a parcel of land (i.e. a nonfinancial asset). Sub B's only asset is an equity method investment (i.e. a financial asset). The fair values of Sub A and Sub B are equal and therefore half of the total value of the assets being sold relates to a nonfinancial asset and the other half relates to a financial asset (and therefore, the equity method investment held by Sub B is not an in-substance nonfinancial asset). In that case, the seller applies Subtopic 610-20 to the sale of the distinct asset within Sub A and applies the relevant US GAAP to the sale of Sub B. See Case C of Example 1 in paragraphs 610-20-55-9 – 55-10. Also, see the flowchart below that describes the scope of Subtopic 610-20. [610-20-15-6]

Section 17.2.40 of KPMG Handbook, Revenue recognition, provides additional discussion, questions, and examples about how to identify in-substance nonfinancial assets.

What about partial sales?

Partial sales of real estate can occur in several ways.

Transaction 1. A seller and a third-party investor form a venture. The seller contributes real estate to the newly formed venture and the third-party investor contributes cash, property or services. The seller retains a controlling financial interest in the venture post-sale and no interest in the third party.

Transaction 2. Assume the same facts as Transaction 1 except the seller retains only a noncontrolling interest in the venture post-sale. The venture may be a joint venture.

Transaction 3. A seller contributes real estate to a newly formed, wholly owned venture. Sometime later, it sells a partial ownership interest in the venture to a third-party investor for cash, property or services. The consideration may come directly from the investor to the seller or may be contributed by the investor to the venture. The seller retains a controlling financial interest in the venture post-sale and no interest in the third party.

Transaction 4. Assume the same facts as Transaction 3 except the seller retains only a noncontrolling interest in the venture post-sale. The venture may be a joint venture.

Transaction 5. A seller transfers real estate to an existing equity method investee in exchange for cash or noncash consideration.

All of these transactions are in the scope of Subtopic 610-20 but the seller has different considerations relative to derecognition and measurement depending on whether it retains a controlling or noncontrolling interest. See Question F90. [610-20-15-3, 323-10-35-7(c), 970-323-30-3]

What isn't in scope?

As previously mentioned, if an asset or a group of assets meets the definition of a business, the seller applies Topic 810 to the derecognition transaction. Subtopic 610-20 also does not apply to:

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

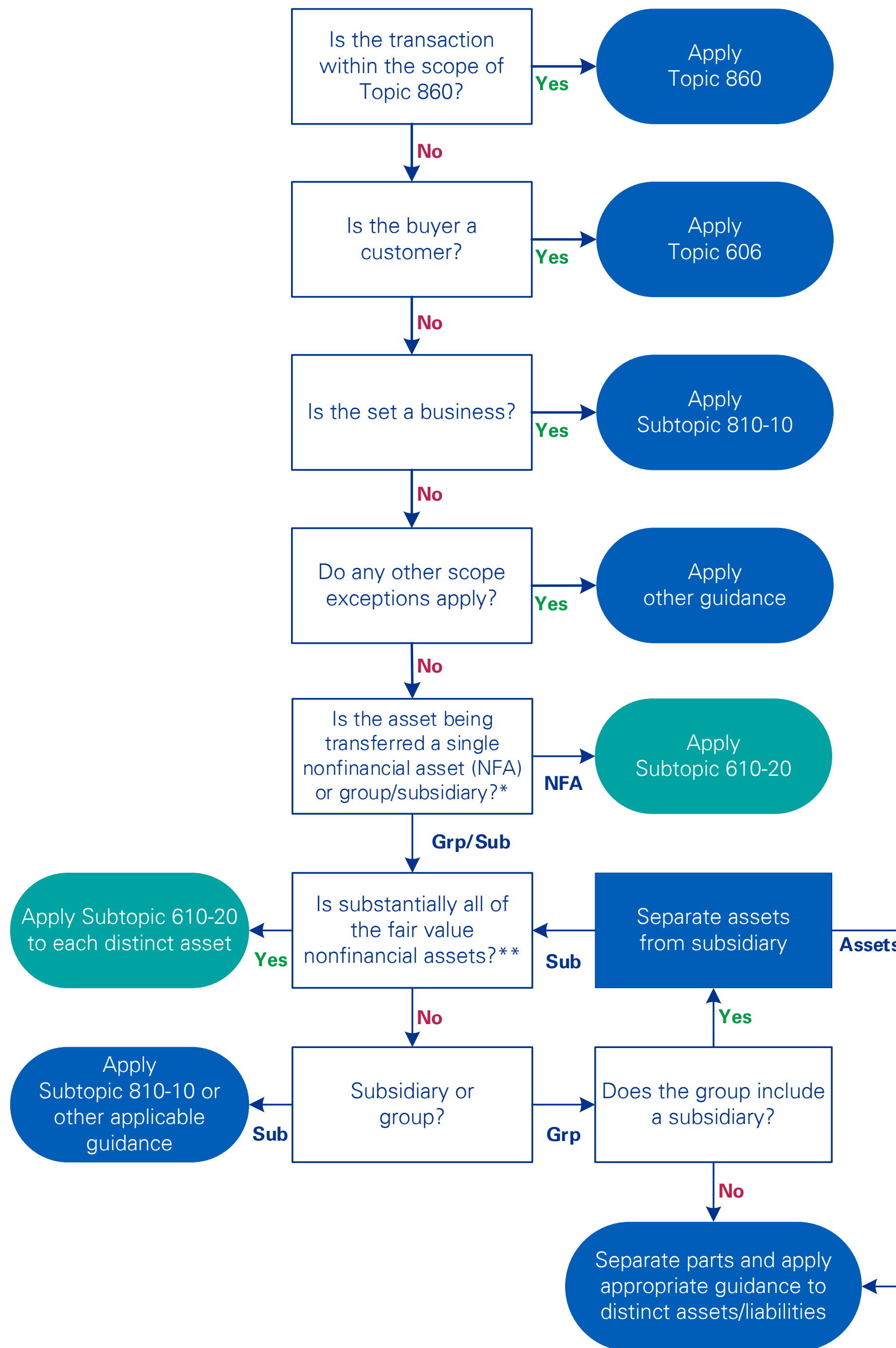
- sales to customers;
- services provided to noncustomers (see Question 17.2.60 of KPMG Handbook, Revenue recognition);
- sales of nonprofit activities;
- transfers of financial assets, including transfers of investments – e.g. those accounted for under the equity method, see Question A25;
- transfers of subsidiaries in which substantially all of the fair value of the assets is *not* concentrated in nonfinancial assets;
- exchanges of nonfinancial assets for a controlling financial interest in a business (business combinations);
- exchanges between entities in the same line of business to facilitate sales to customers;
- nonreciprocal transfers;
- sale-leaseback transactions (see discussion that follows);
- lease contracts;
- contributions made that are within the scope of Subtopic 720-25 (other expenses – contributions made) or Subtopic 958-605 (not-for-profit entities – revenue recognition);
- transfers of investments in ventures accounted for using proportionate consolidation as described in paragraph 810-10-45-14;
- transfers between entities under common control;
- conveyances of oil and gas mineral rights; and
- exchanges of airline take-off and landing slots. [610-20-15-4]

How does a seller determine what guidance applies when transferring a nonfinancial asset?

The following decision tree summarizes the sequence of analysis required to evaluate which guidance applies for a transaction that entirely, or partially, involves a nonfinancial asset.

This decision tree may be more useful in more complicated transactions (mix of financial and nonfinancial assets).

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.



* If the transfer includes other contractual arrangements that are not the assets of the seller that will be derecognized (e.g. guarantees), those contracts are separated and accounted for under the applicable guidance. See Section 17.2.60 of KPMG Handbook, Revenue recognition, for additional guidance.

** See Section 17.2.40 of KPMG Handbook, Revenue recognition, for additional guidance.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

What guidance applies to a real estate sale-leaseback if Subtopic 610-20 does not?

Seller/lessee applying Topic 840

Subtopic 610-20 does not apply to real estate sale-leaseback transactions; those transactions remain in the scope of Subtopics 840-40 and 360-20 until the new leases guidance (Topic 842) is applied. Therefore, sale-leaseback accounting is not changed when a company adopts Subtopic 610-20 until it adopts Topic 842. [610-20-15-4(c)]

For example, assume a calendar year-end private company adopts Subtopic 610-20 on January 1, 2020 and adopts Topic 842 on January 1, 2022. In its 2021 and 2020 financial statements, the company continues to apply Subtopics 840-40 and 360-20 to any real estate sale-leasebacks for which it is the seller-lessee. The company's adoption of Subtopic 610-20 on January 1, 2020 does not change how it accounts for these transactions as compared with transactions entered into before that date.

Subtopic 840-40 does not require a seller-lessee entering into sale-leaseback transactions for assets other than real estate or integral equipment to evaluate the pre-Subtopic 610-20 other income guidance in US GAAP. Therefore, the accounting for sale-leaseback transactions of those assets is unaffected by the adoption of Subtopic 610-20.

Seller/lessee applying Topic 842

Topic 842 supersedes all of Topic 840, including Subtopic 840-40, and also supersedes the sale-leaseback provisions in Subtopic 360-20 that continued to apply even after a company's adoption of Topic 606/Subtopic 610-20. Therefore, on adopting Topic 842 a seller-lessee will no longer apply Subtopics 840-40 and 360-20 to its sale-leaseback transactions. Topic 842 provides a single accounting model for sale-leaseback transactions that applies regardless of the type of asset transferred.[3]

The seller-lessee **and the buyer-lessor** in a sale-leaseback transaction consider the guidance in Topic 606 (and the other specific sale/purchase requirements in Subtopic 842-40) to assess whether a sale/purchase of the asset has occurred. The company then applies the lease guidance in Topic 842 when accounting for the leaseback (or the failed sale-leaseback guidance in Subtopic 842-40 if a sale/purchase has not occurred).

Question A21
Does Subtopic 610-20 apply to the transfer of an option to purchase real estate?

Background: A transferor applies Subtopic 610-20 when it derecognizes nonfinancial assets. Nonfinancial assets include intangible assets, land, buildings, or materials and supplies. [610-20-15-2]

3 For more information on sale-leaseback transactions, see KPMG Handbook, Leases.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

A transferor applies Topic 860 (transfers and servicing) when it derecognizes financial assets and analogizes to Topic 860 when it derecognizes derivative assets that are not financial assets – e.g. derivatives that require physical delivery of a nonfinancial asset that is readily convertible to cash (and therefore meets the net settlement criterion). [860-10-15-3 – 15-5, 815-10-40-1 – 40-3, 15-119 – 15-139]

The Master Glossary to the Codification defines a financial asset as cash, evidence of an ownership interest in an entity, or a contract that conveys to one entity a right to do either of the following: [Master Glossary]

- receive cash or another financial instrument from a second entity; or
- exchange other financial instruments on potentially favorable terms with the second entity.

Topic 815 (derivatives and hedging) defines a derivative instrument as a financial instrument or other contract with all three of the following characteristics. [815-10-15-83]

- It has (1) one or more underlyings and (2) one or more notional amounts or payment provisions or both.
- It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors.
- Its terms require or permit net settlement, it can readily be settled net by a means outside the contract, or it provides for delivery of an asset that puts the recipient in a position not substantially different from net settlement.

However, Topic 815 excludes from its scope a contract that meets the definition of a derivative if it is: [815-10-15-59]

- not exchange-traded;
- the underlying on which the settlement is based is the price or value of a nonfinancial asset of one of the parties to the contract; and
- the nonfinancial asset is not readily convertible to cash.

Interpretive response: Generally, yes. A transferor applies Subtopic 610-20 when derecognizing an option to purchase real estate unless the option is a financial asset or a derivative within the scope of Topic 815.

We believe a real estate option is rarely a financial asset, because it generally does not give the holder the right to receive cash or a financial instrument.

We also believe a real estate option is rarely a derivative within the scope of Topic 815, because generally:

- it does not meet the definition of a derivative because it requires physical delivery of real estate; or
- it meets the exclusion from derivative accounting for contracts that meet the definition of a derivative but are not traded on an exchange.

If a transferor transfers (sells or assigns) an option to purchase real estate or other asset to a buyer and then leases that asset back from the buyer, the transfer and leaseback may be considered to be a sale-leaseback transaction that should be accounted for based on the guidance in Subtopic 842-40. Refer to the sale-leaseback discussion in Question A20 and Chapter 9 of KPMG Handbook, Leases, including Question 9.1.15 on determining when the transfer

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

of an option and leaseback of the asset subject to the option is within the scope of 842-40.

Question A25

What guidance should a seller apply when it sells a noncontrolling interest in an entity that is not a subsidiary (e.g. equity method investee)?

Interpretive response: As discussed in Question A20, Subtopic 610-20 does not apply to transfers of financial assets, including transfers of investments – e.g. those accounted for under the equity method. The scope of Topic 860 applies to the sale of those investments regardless of whether (a) the buyer is a customer or a noncustomer, and (b) the underlying assets are predominantly real estate or other nonfinancial assets. [610-20-15-4(e)]

However, if an entity sells its 100% ownership in a subsidiary that is not a business to a noncustomer and the fair value of the assets within that subsidiary is concentrated in nonfinancial assets, then the seller applies Subtopic 610-20 to the sale of each of the assets within the subsidiary. This includes any financial assets (like equity method investments) because those financial assets are in-substance nonfinancial assets. See Question A20. [610-20-15-7]

Question A26

Are sales of undivided interests to noncustomers in the scope of Subtopic 610-20? What if the buyer is a customer?

Interpretive response: It depends. While Subtopic 610-20 does not address whether transfers of undivided interests are within its scope, we believe sellers should apply it to transfers when the undivided interest being sold is accounted for as a nonfinancial asset. Likewise, we believe sellers should apply Subtopic 610-20 to transfers of undivided interests in nonfinancial assets that were wholly owned before the sale.

Some entities account for undivided interests in legal entities under the equity method, but use gross financial statement presentation, often referred to as proportionate consolidation. Subtopic 610-20 excludes sales of both equity method investments and undivided interests in ventures when proportionate consolidation is used. These investors should apply Topic 860 to derecognition events. See Question A25. [610-20-15-4]

Undivided interests in unincorporated legal entities

Subtopic 323-30 generally requires an investor with an interest in a partnership or unincorporated joint venture (also referred to as **undivided interests in ventures**) to account for it under the equity method if the investor has significant influence over the investee. The SEC staff's position is that these investors should apply the equity method unless their interests are so minor that they have virtually no influence. General partners are presumed to have interests that are more than minor. In practice, limited partners generally are

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

presumed to have interests that are more than minor when their equity interests are more than 3 to 5%. [323-30-15-2 – 15-3, 25-1, 323-30-S99-1, 970-323-25-2, 25-6]

There are narrow exceptions to the guidance in Subtopic 323-30. Subtopics 910-810, 930-810 and 932-810 each provide an exception for interests in investees in the construction or extractive industries when the investor also is in those industries. For those investments, the investor applies the recognition and measurement guidance for equity method investments as described in Topic 323 (equity method and joint ventures). However, the investor is permitted to apply gross, or proportionate, presentation in the financial statements versus the one-line presentation required by Topic 323. [910-810-45-1, 930-810-45-1, 932-810-45-1, 810-10-45-14]

As discussed above, Subtopic 610-20 excludes sales of equity method investments and investments in ventures accounted for using proportionate consolidation. We believe that investors with undivided interests in ventures, including those investors that present the assets and liabilities underlying the venture on a gross basis, should apply Topic 860 for derecognition. While some investors have the option for gross presentation versus one-line **presentation**, all must apply the recognition and measurement guidance for equity method investments.

Undivided interests in nonfinancial assets – non-real property

Undivided interests[4] in specific assets or liabilities generally are outside the scope of Topic 323 because they represent direct proportional ownership of individual assets or liabilities versus ownership in an entity holding the assets or liabilities. Investors with undivided interests in specific assets that are not real property generally separately account for their share of those assets. Investors with undivided interests in real property must meet certain criteria to separately account for their share of the assets (see below).

We believe that investors with undivided interests in nonfinancial assets that separately account for their proportionate ownership should apply Subtopic 610-20 for derecognition. We do not believe these proportionate ownership interests are outside the scope of Subtopic 610-20 because they are not accounted for under paragraph 810-10-45-14. See Question A20.

Likewise, we believe sellers should apply Subtopic 610-20 to transfers of undivided interests in nonfinancial assets that were wholly owned before the sale. When a seller transfers an undivided interest and retains an undivided interest that is accounted for as a nonfinancial asset, we believe the asset being sold – i.e. the unit of account to which Subtopic 610-20 is applied – is the proportionate ownership interest in the asset. We do not believe the retained proportionate ownership interest in the asset (which continues to be accounted for as a nonfinancial asset) represents consideration received for the sale. Thus, the retained proportionate ownership interest in the asset would not be remeasured to fair value.

---

[4] An undivided interest is defined in Subtopic 970-810 as an ownership arrangement in which two or more parties jointly own property, and title is held individually to the extent of each party's interest.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Undivided interests in real property

Subtopic 970-323 requires an investor with an undivided interest in real property to account for its interest under the equity method if the real property is subject to joint control. Investors have joint control when decisions about the financing, development, sale and operations of the real estate require the approval of two or more of the investors. [970-323-25-12]

If the investors do not have joint control, they may separately account for their share of the assets, liabilities, revenue and expenses if the following additional conditions are met:

- each investor is entitled to only its pro rata share of income;
- each investor is responsible to pay only its pro rata share of expenses; and
- each investor is severally liable only for indebtedness it incurs in connection with its interest in the property. [970-810-45-1]

We believe that investors with undivided interests in real property that separately account for their proportionate ownership of those assets should apply Subtopic 610-20 for derecognition of those undivided interests. We do not believe these proportionate ownership interests are outside the scope of Subtopic 610-20 because they are not accounted for under paragraph 810-10-45-14.

Likewise, we believe sellers should apply Subtopic 610-20 to transfers of undivided interests in real property that was wholly owned before the sale; however, we believe the application of Subtopic 610-20 depends on the seller's characterization of the retained interest in the asset after the sale.

When a seller transfers an undivided interest and retains an undivided interest that is accounted for as a nonfinancial asset, we believe the asset being sold – i.e. the unit of account to which Subtopic 610-20 is applied – is the proportionate ownership interest in the asset. We do not believe the retained proportionate ownership interest in the asset (which continues to be accounted for as real property) represents consideration received for the sale. Thus, the retained proportionate ownership interest in the real property would not be remeasured to fair value. This is consistent with the FASB's statement that it is not appropriate to remeasure a retained interest when the asset does not change its character from a nonfinancial asset to a financial asset. [ASU 2017-05.BC64]

When a seller transfers an undivided interest and retains an undivided interest that is accounted for as an equity method investment, we believe the asset being sold – i.e. the unit of account to which Subtopic 610-20 is applied – is the entire asset. We believe the equity method investment represents noncash consideration received for the sale. Thus, the equity method investment would be initially measured at fair value just as retained equity method investments are in partial sale transactions. See additional discussion in Question F90.

While proportionate accounting for the undivided interest in real property may be applied when the above conditions are met, the investor may alternatively elect to apply the equity method. If the investor elects to account for its interest under the equity method, we believe it should apply Topic 860 for derecognition. See Question A25.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Sales to customers

Sales of undivided interests to customers are in the scope of Topic 606 unless the undivided interest is in-substance a financial asset. Sales of financial assets are accounted for under Topic 860 regardless of whether the buyer is a customer. In the real estate industry, we believe many sales of undivided interests to customers (e.g. time-sharing interests) should be accounted for under Topic 606. See Question C10.

Question A30

How does an entity apply the revenue (or other income) recognition guidance when it sells property improvements (or integral equipment) and leases the underlying land to a customer?

Interpretive response: When a contract contains elements covered by different accounting Topics, the entity applies the guidance in those other Topics about how to separate and/or initially measure those elements. However, if the other guidance does not specify how to separate and/or initially measure one or more parts of the contract, then the entity applies Topic 606's separation and/or measurement guidance. [606-10-15-4, 610-20-15-19]

Seller/lessor applying Topic 840

The guidance on accounting for leases (Topic 840) requires the seller/lessor to separate lease and non-lease components on a relative stand-alone selling price basis. For example, in a sale of improvements together with a lease of the land on which the improvements are located, the seller/lessor separates the transaction into the lease of the land and the sale of the improvements and accounts for each separately. Revenue or gain is recognized on the sale of the property improvements (or integral equipment) when control transfers to the customer (based on the requirements in Topic 606 or Subtopic 610-20). The lease of the land is accounted for under Topic 840, which requires lessors to classify land leases as operating leases if there is no automatic transfer of title to the lessee by the end of the lease term. [840-10-15-17 – 15-19, 606-10-32-28 – 32-41, 610-20-32-6]

Because Topic 840 generally addresses separation and measurement in transactions with lease and non-lease components regardless of whether the lessee is a customer, this guidance applies to both transactions with customers and noncustomers. However, the presentation of the sale transaction is treated differently. Subtopic 610-20 requires gain/loss presentation for noncustomer transactions while Topic 606 requires revenue and cost of sales presentation for customer transactions.

Topic 842, *Leases*[5] supersedes Topic 840 once effective. The following are the effective dates for Topic 842.

---

5 For more information on Topic 842, see KPMG Handbook, Leases.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

	Public business entities[6]	Public not-for-profit entities[7, 8]	Other entities
Effective date	Annual and interim periods in fiscal years beginning after December 15, 2018	Annual and interim periods in fiscal years beginning after December 15, 2019	— Annual periods in fiscal years beginning after December 15, 2021 — Interim periods in fiscal years beginning after December 15, 2022

Seller/lessor applying Topic 842

Topic 842, like Topic 840, includes guidance on separating lease and non-lease components. A lessor must separate a single contract into each separate lease and non-lease component and allocate the consideration in the contract using the transaction price allocation guidance in Topic 606. Thus, the contract consideration usually is allocated on a relative stand-alone selling price basis. Topic 842 offers lessors a practical expedient not to separate lease and non-lease components if specific criteria are met (see Question G20 for additional information). However, we believe a sale of property improvements with an accompanying lease of the underlying land generally would not qualify. [606-10-32-28 – 32-41, 842-10-15-28 – 15-32, 15-38 – 15-42]

Topic 842 requires a lessor to classify a lease as an operating lease unless the lessee:

a. effectively obtains control of the underlying asset as a result of the lease by meeting one of the five criteria outlined below; or
b. does not obtain effective control but:
   - the present value of the sum of the lease payments **plus**
   - any residual value guaranteed by the lessee (or any other third party unrelated to the lessor) not already reflected in the lease payments
   - **equals** or **exceeds** substantially all of the fair value of the underlying asset *and* it is probable that the lessor will collect the lease payments plus the amount needed to satisfy the residual value guarantee. [842-10-25-2 – 25-3]

A lessee effectively obtains control of the underlying asset when the lease meets any of the following criteria at lease commencement: [842-10-25-2, 842-10-55-2 – 55-7]

a. the lease transfers ownership of the underlying asset to the lessee by the end of the lease term;

---

6 This includes (1) public business entities, (2) public not-for-profit entities not addressed by Note 9, and (2) employee benefit plans that file or furnish financial statements with or to the SEC.

7 'Public' not-for-profit entities are those that have issued, or are conduit bond obligors for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market.

8 Public not-for-profit entities are eligible to elect this effective date if they did not issue GAAP-compliant financial statements reflecting the adoption of Topic 842 before June 3, 2020 (the issuance date of ASU 2020-05).

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

b. the lease grants the lessee an option to purchase the underlying asset that the lessee is reasonably certain to exercise;
c. the lease term is for the major part of the remaining economic life of the underlying asset, assuming the commencement date does not fall at or near the end of the economic life of the underlying asset;
d. the present value of the sum of the lease payments and any residual value guaranteed by the lessee that is not already reflected in the lease payments equals or exceeds substantially all of the fair value of the underlying asset; or
e. the underlying asset is so specialized that it is expected to have no alternative use to the lessor at the end of the lease term.

Question A40

How do guarantees affect the accounting for an accompanying sale of real estate?

Interpretive response: When a contract with a customer or noncustomer contains elements addressed by different Topics, if the other Topics specify how to separate and/or initially measure one or more parts of the contract, then an entity first applies those separation and/or initial measurement requirements. [606-10-15-2, 15-4, 610-20-15-9, 55-2 – 55-5]

The seller first determines whether Topic 460 (guarantees), Topic 815 (derivatives and hedging) or another Topic applies to the guarantee. If the guarantee is within the scope of Topic 460 or Topic 815 (see KPMG Handbook, Derivatives and hedging), the seller/guarantor initially recognizes and measures it at fair value using the initial measurement guidance in the applicable Topic. The seller then allocates the remainder of the consideration to the sale of the property. [606-10-15-2, 610-20-15-9]

The following guarantee contracts are within the scope of Topic 460.

a. Contracts that contingently require a guarantor to make payments to a guaranteed party based on changes in an underlying that is related to an asset, a liability, or an equity security of the guaranteed party.
b. Contracts that contingently require a guarantor to make payments to a guaranteed party based on another entity's failure to perform under an obligating agreement (performance guarantees).
c. Indemnification agreements (contracts) that contingently require a guarantor to make payments to an indemnified party (guaranteed party) based on changes in an underlying that is related to an asset, a liability, or an equity security of the indemnified party.
d. Indirect guarantees of the indebtedness of others, even though the payment to the guaranteed party may not be based on changes in an underlying that is related to an asset, a liability, or an equity security of the guaranteed party. [460-10-15-4]

Topic 460's implementation guidance states that a market value guarantee on a nonfinancial asset owned by the guaranteed party is an example of the type of contract described in (a) above. We believe a seller's guarantee of a buyer's investment (or a return on its investment), similar to a market value guarantees, generally falls within the scope of Topic 460 and is separated from the sale

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

transaction and initially measured at fair value. The seller allocates the remainder of the contract consideration to the sale of the real estate, which is subject to Topic 606's guidance on determining the transaction price. [460-10-15-4(a), 55-2(b)]

Because the seller accounts for it separately, the guarantee does not affect the seller's ability to recognize revenue or gain when it transfers control of the real estate to the buyer. Guarantee-like arrangements not within the scope of Topic 460 or other accounting guidance are combined with the sale transaction that is accounted for under Topic 606 or Subtopic 610-20. These guarantee-like provisions may affect the:

a. amount of revenue, gain or loss recognized on the sale (because the provision may result in the transaction price being variable); or
b. timing of derecognition if the provision is significant enough to conclude that control of the property has not transferred.

See Question F10 for discussion about control transfer.

For example, an entity may guarantee its own performance. Consider a seller/developer that sells land with an accompanying construction contract and concludes it is a single performance obligation (see Question C20). The seller/developer may provide a service-related guarantee that requires it to pay a penalty if not fulfilled. Because the seller/developer is guaranteeing its own performance, that provision is not in the scope of Topic 460. Instead, it gives rise to variable consideration.

Refer to Question 2.3.10 of KPMG Handbook, Revenue recognition, for additional guidance on guarantees of an entity's own future performance. See also Question F60 in this publication for discussion of put options, which, like some guarantee provisions, may result in a seller retaining control despite relinquishing physical possession of the property.

Question A50

How do support obligations affect the accounting for an accompanying sale of real estate?

Interpretive response: If the seller's obligation to support the operations of the property (e.g. the seller agrees to support the operations up to a break-even level of cash flows for a period of time) is within the scope of Topic 460, the seller separates the support obligation and initially recognizes and measures it at fair value under Topic 460's initial measurement guidance. The seller allocates the remainder of the contract consideration to the sale of the real estate. [460-10-30-2]

In our experience, support obligations generally have the characteristics of guarantees that are within the scope of Topic 460, because they are analogous to guarantees of the collection of scheduled contractual cash flows from financial assets or business revenue. [460-10-15-4(a), 55-2(d) – 55-2(e)]

Therefore, we believe most support obligations should be separated from the sale transaction and initially measured at the fair value of the guarantee. When the seller accounts for a support obligation separately, the obligation does not

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

affect the seller's ability to recognize revenue or gain when the seller transfers control of the real estate to the buyer.

Guarantee-like arrangements not within the scope of Topic 460 or other Topics remain combined with the sale transaction and may affect the:

a. amount of revenue, gain or loss recognized on the sale (because the provision may result in the transaction price being variable); or
b. timing of derecognition if the provision is significant enough to conclude that control of the property has not transferred.

See Question F10 for discussion about control transfer and Question F60 for discussion about put options, which is another situation in which a seller may retain control despite relinquishing physical possession of the property.

Example A50.1
Property sale with support obligation

Description of the arrangement

ABC Corp. sells a newly constructed property with a cost of $1,200,000 to DEF Corp. for $2,000,000 in cash. ABC guarantees the cash flows of the property will be sufficient to meet all the property's operating needs for the first three years after the sale date. The fair value of the guarantee at the sale date is $30,000 and there is no other variable consideration.

Evaluation

Because the support obligation is a guarantee within the scope of Topic 460, it is initially separated from the real estate sale and measured at fair value. ABC allocates $30,000 of the $2,000,000 contract consideration to the guarantee, and allocates $1,970,000 to the sale of the property, which is the transaction price.

ABC recognizes a profit of $770,000 ($1,970,000 less $1,200,000 cost) when it transfers control of the property. The guarantee continues to be accounted for separately under Topic 460 and does not affect the profit recognized on the sale. ABC recognizes subsequent changes in the guarantee's carrying amount outside of revenue (or gain on sale if the buyer is not a customer).

Question A60
Under Topic 606, what is the unit of account for sales of condominium units within a condominium project (or similar structure)?

Interpretive response: Topic 606 generally specifies the unit of account is an individual contract with a customer and includes implementation guidance that illustrates individual contracts with customers to construct individual units in a multi-unit residential complex are accounted for separately. [606-10-55-180]

However, there is a practical expedient that allows an entity to apply the guidance to a portfolio of contracts (or performance obligations) with similar

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

characteristics, but only if the entity reasonably expects the effect on the financial statements to not differ materially from applying the guidance to the individual contracts. [606-10-10-4]

We believe it may be difficult for an entity to demonstrate a reasonable expectation that the effect of using a project or portfolio approach is materially the same as using an individual contract approach because the:

a. control of the individual units likely will transfer at different points in time (see Question F40 about the pattern of control transfer in unit sales); and
b. transaction prices and fulfillment costs of individual units within a project likely will be different.

Question A70

Is a property or asset manager's carried interest (or promote) in the scope of Topic 606?

Interpretive response: It depends.

Managers are compensated in different ways for providing asset management services including a base management fee, an incentive-based fee or an incentive-based capital allocation in the form of a carried interest in a partnership or similar structure. Incentives are earned based on the performance of the assets under management.

Under legacy GAAP, if a general partner (manager) did not consolidate the limited partnership, it generally accounted for its fee (including its performance fee in the form of a carried interest) based on the guidance in paragraph 605-20-S99-1 (previously EITF Topic D-96), which provided two acceptable methods for income recognition. Topic D-96 also included guidance that permitted entities that previously applied the equity method to these arrangements to continue to do so. Because this guidance was to be withdrawn by the SEC when Topic 606 became effective, stakeholders raised questions about whether carried interest arrangements are within the scope of Topic 606 or, because generally they are in the legal form of equity, they should be accounted for as an ownership interest in the investee entity.

The IASB and FASB's Joint Transition Resource Group for Revenue Recognition discussed this issue at its April 2016 meeting. FASB members present at the meeting indicated that the FASB discussed performance fees in asset management contracts when developing Topic 606. All FASB members present at the meeting expressed the view that performance fees in the form of carried interest arrangements were intended to be within the scope of Topic 606. [TRG 04-16.50]

The SEC Observer at the meeting indicated that the SEC staff would accept an application of Topic 606 for these arrangements. However, he also noted that applying an ownership model to these arrangements, rather than Topic 606, may be acceptable based on the specific facts and circumstances. If an entity were to apply an ownership model, the SEC staff would expect the full application of the ownership model, including an analysis of the consolidation guidance in Topic 810, the equity method of accounting under Topic 323 or other relevant guidance. We understand that the SEC staff would not object to

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

the view that the carried interest would be evaluated as a **performance fee** rather than an interest in the fund itself when making an assessment of whether it is a variable interest under Topic 810.

The SEC Observer did not elaborate on the nature of the facts and circumstances that in the SEC staff's view would require application of Topic 606 to these arrangements. We are not aware of any examples in which the SEC staff believes applying an ownership model would be unacceptable when the performance fee is in the form of equity (i.e. carried interest).

Based on our understanding of the SEC staff's views, we believe both private and public companies may make an accounting policy election when they adopt Topic 606 to account for performance-based fees in the form of a capital allocation by applying either:

- the revenue recognition guidance in Topic 606; or
- an equity ownership model using the guidance in Topic 323, Topic 810 or other relevant guidance.

Either accounting policy selected should be consistently applied. Based on our current understanding of the views of the FASB and SEC staff, if an entity elects to initially apply Topic 606 to these arrangements, we believe generally it will be difficult to support a conclusion that it is preferable to change to an ownership model at a future date. Our current understanding may be affected by future standard setting or regulatory developments that may cause our views to change.

If an entity determines it is appropriate to apply an ownership model (e.g. Topic 323) it applies the guidance in Topic 250 (accounting changes and error corrections) for a change in accounting and not the transition guidance in Topic 606. In that case, presentation and disclosure of the equity income from these arrangements would also be separated from revenue from arrangements that are accounted for under Topic 606.

See chapter 3 of KPMG Handbook, Accounting changes and error corrections, for additional guidance on accounting changes.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

B. Step 1: Identify the contract

Question

Q&A B10 What consideration should a seller give to the buyer's initial and continuing investments when evaluating if a contract exists?

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question B10

What consideration should a seller give to the buyer's initial and continuing investments when evaluating if a contract exists?

Interpretive response: Subtopic 610-20 requires an entity to apply the guidance in Topic 606 to determine if the agreement meets the contract existence criteria. These criteria establish the enforceable rights and obligations of a contract and include the following (all must be met):

a. parties have approved the contract and are committed to performing their respective obligations;

b. entity can identify each party's rights regarding the goods or services to be transferred;

c. entity can identify the payment terms for the goods or services to be transferred;

d. contract has commercial substantive; and

e. it is probable that the entity will collect substantially all of the consideration to which it will be entitled.

Refer to Sections 3.2 and 3.3 of KPMG Handbook, Revenue recognition, for further guidance on determining whether a contract exists and applying the collectibility criterion, respectively. [610-20-25-5, 606-10-25-1 – 25-8]

Unlike legacy guidance for real estate sales, neither Topic 606 nor Subtopic 610-20 require that the buyer provide specific levels of initial or continuing investment to demonstrate that the contract existence criteria are met.

The objective of evaluating the buyer's ability and intention to pay is to assess whether there is a substantive transaction between the seller and the buyer. This assessment is partially forward looking, which requires the seller to use judgment and consider all facts and circumstances, including the seller's customary business practices and its knowledge of the buyer.

Seller's considerations when evaluating whether collectibility is probable	

Payment terms that suggest a significant uncertainty about the buyer's intention and ability to fulfill its obligations	Do the payment terms reflect inherent uncertainty about the buyer's intention to fulfill its obligations?
	— Small down payment relative to the overall contracted price.
	— Nonrecourse, seller-provided financing.
	— Customer-provided collateral or guarantees that are illiquid or have highly variable or unobservable fair value.
	— Continuing periodic payments that extend beyond:
	  – a customary financing period for similar transactions; and
	  – the property's estimated useful life.
	— No periodic payments required.
	— Guarantees provided by lower-rated counterparties.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Seller's considerations when evaluating whether collectibility is probable	
Importance of the property to the buyer's operations	— Does the buyer's business model and reasons for entering into the transaction raise doubt about its intention to follow through with its obligations? — Does the buyer need the property to operate its business, which likely indicates that it would have a greater commitment to perform than if the purchase was made for speculative investment purposes?
Prior experience	— Does the seller have prior experience with the buyer (or a similar class of buyer) for the same or similar transaction that raises questions about the buyer's intent and ability to perform? — Has the seller previously chosen not to enforce its contractual rights in similar contracts with the buyer (or buyer class) under similar circumstances? — Is the seller's receivable subject to future subordination?

An entity should not view these factors in isolation. Instead, the entity should evaluate the factors collectively and evaluate all relevant facts and circumstances. No single factor determines whether the buyer is committed to perform or collectibility is probable. An entity that refers to the legacy guidance in Subtopic 360-20 on initial and continuing investments as an indicator of whether collectibility is probable should not consider these thresholds as safe harbors or bright lines. The seller's ability to later repossess the property after it transfers control to the buyer at a point in time should not be considered when assessing its ability to mitigate its credit risk exposure. [606-10-55-3C]

If a contract does not exist, the seller:

- continues to report the nonfinancial asset on its statement of financial position;
- depreciates it if it is not held for sale; and
- evaluates it for impairment as necessary under Section 360-10-35. [606-10-25-1, 610-20-25-5, 360-10-40-3C, 45-9 – 45-10]

The seller then accounts for cash collected as a deposit liability until a contract exists and the seller transfers control of the property or until the seller meets one of these conditions:

a. the seller has no remaining obligations to transfer goods or services to the customer and all, or substantially all, of the promised consideration has been received and is nonrefundable;

b. the contract has been terminated, and the consideration received is nonrefundable; or

c. the seller has transferred control of the goods or services for which it has received consideration; the seller has stopped transferring goods and services to the buyer (if applicable) and has no obligation under the contract to transfer additional goods or services; and the consideration received from the buyer is nonrefundable. [610-20-25-5, 606-10-25-6 – 25-8]

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

If facts and circumstances change and the seller can subsequently demonstrate that a contract exists or one of the conditions above are met, it will recognize revenue under Topic 606 (customer transactions) or gain under Subtopic 610-20 (noncustomer transactions).

Topic 606 illustrates the collectibility analysis in the context of a real estate sale when a real estate developer sells a building and provides long-term, nonrecourse financing for 95% of the sales price. The buyer expects to repay the loan primarily from income derived from its restaurant business and lacks other income or assets to repay the loan. Additionally, the restaurant business faces significant competitive risks and the buyer has limited industry experience. Because of the uncertainty associated with the buyer's ability and intention to pay, the seller concludes that the criteria necessary to conclude a contract exists are not met. [606-10-55-95 – 55-98, 25-1]

At the sale date (and each reporting period), the seller must evaluate the conditions necessary to conclude a contract exists (or one of the conditions in paragraph 606-10-35-7 is met) to determine how to account for the nonrefundable deposit. [606-10-25-1 – 25-8, 610-20-25-5]

We believe at the sale date the seller in the above fact pattern likely would not recognize revenue or gain because:

- it is not probable the seller will collect the consideration to which it is entitled;
- the seller has not received substantially all of the consideration;
- the seller provided nonrecourse financing for a substantial portion of the consideration;
- the contract has not been terminated; and
- the seller may not have transferred control of the building (see Question F10).

Until the seller can conclude a contract exists or one of the conditions in paragraph 606-10-25-7 is met, it does not derecognize the asset or recognize a receivable. The seller instead will recognize the nonrefundable deposit received as a deposit liability. [606-10-25-30, 610-20-25-5, 360-10-40-3C]

The seller must continue to assess the contract to determine if and when it is appropriate to recognize revenue or gain. We believe the following situations will most commonly occur in real estate sales when a contract does not exist at the sale date.

- A contract subsequently does exist because the buyer has established a consistent payment history, obtained other capital or financing sources, or accumulated sufficient funds to reduce the risk of nonpayment. The seller derecognizes the building and recognizes revenue or gain on the sale at the point in time control transfers. [606-10-25-1]

- A contract does not exist, but the parties terminate the arrangement and the seller repossesses the property. The seller recognizes the nonrefundable deposit in income. [606-10-25-1 – 25-8, 610-20-25-5]

The guidance on evaluating the existence of a contract (and the accounting if a contract does not exist) applies to both customer and noncustomer transactions.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

C. Step 2: Identify the performance obligations

Questions

Q&A C10	Is the sale of an undivided interest in the common areas where the seller/developer may build future amenities considered a separate performance obligation from the sale of a condominium unit or residential lot when the undivided interest is transferred to the customer in the sales transaction? Does the answer change if the seller/developer does not transfer the undivided interest but will transfer future amenities to a third party?
Q&A C15	What is the unit of account for noncustomer real estate sales when the disposal group includes more than one asset?
Q&A C20	Does the sale of land and the agreement to construct property improvements comprise multiple performance obligations? Is the analysis different if the buyer is not a customer?
Q&A C30	How should an entity analyze the number of performance obligations in a typical property management services contract?

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question C10

Is the sale of an undivided interest in the common areas where the seller/developer may build future amenities considered a separate performance obligation from the sale of a condominium unit or residential lot when the undivided interest is transferred to the customer in the sales transaction? Does the answer change if the seller/developer does not transfer the undivided interest but will transfer future amenities to a third party?

Interpretive response:

Transferring future amenities to the customer

A seller accounts for a good or service as a performance obligation if the good or service promised to the customer is distinct from other goods or services promised in the contract. A good or service is distinct if:

a. the customer can benefit from the good or service either on its own or with other resources that are readily available to the customer (i.e. the good or service is capable of being distinct); and
b. the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (i.e. distinct in the context of the contract). [606-10-25-19]

Capable of being distinct

A good or service meets criterion (a), capable of being distinct, if it could be "used, consumed, sold for an amount that is greater than scrap value, or otherwise held in a way that generates economic benefits." The fact that the entity regularly sells a good or service separately indicates that a customer could benefit from the good or service on its own or with other readily available resources. [606-10-25-20]

Distinct in the context of the contract

The seller's objective when assessing whether a promise is distinct in the context of the contract (criterion (b)) is to determine whether the nature of its overall promise is to transfer each of the goods or services, or whether the promise is to transfer a combined item to which each of the promised goods or services are inputs. [606-10-25-21]

These factors indicate a good or service is not distinct in the context of the contract:

— the entity provides a significant service of integrating the goods or services with other goods or services promised in the contract;

— one or more of the goods or services significantly modifies or customizes, or is significantly modified or customized by, one or more of the other goods or services promised in the contract; or

— the goods or services are highly interdependent or highly interrelated – i.e. each one is significantly affected by the other goods or services.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

The undivided interest in the common areas, regardless of whether the amenities have been completed, generally:

a. cannot generate independent economic benefits to the buyer (the undivided interest is not practically separable from the fee interest in the unit or lot); and

b. is integral to the buyer's purchase of the unit or lot – i.e. the buyer is unable to purchase (or not purchase) the undivided interest in the common areas without the condominium unit or lot.

Therefore, we believe the sale of the unit or lot and the accompanying transfer to the customer of the undivided interest in the common areas would be a single performance obligation.

We believe this conclusion is consistent with the FASB's guidance stating that a developer may need to include construction of common areas in its measure of progress toward completely satisfying its performance obligation to construct an individual unit within a multi-unit residential complex. [606-10-55-180]

We also believe this conclusion is consistent with the cost guidance in Subtopic 970-340 that requires developers to allocate to the benefitted land parcels the common costs of the amenity. This guidance was not amended by Topic 606 or Topic 340 (other assets).

Accounting for amenity costs – amenity transferred to the customer

The FASB's industry guidance in Subtopic 970-340 on accounting for amenity costs applies because the future amenity is being sold or transferred in connection with the sale of individual units by transferring the undivided interest to the customer. In this situation, the developer should allocate the costs that exceed the anticipated proceeds as common costs to the land parcels that benefitted from the development, or probably will benefit, because the amenity is clearly associated with the sale of the project. The common costs include the developer's expected future operating costs until the amenity is assumed by the buyers of the units. Before the amenity is substantially complete and available for use, operating income (loss) is included as a reduction of (or addition to) common costs. See additional discussion in Question F40 about the timing of revenue recognition for sales of condominium units (and other similar structures). [970-340-25-9 – 25-11]

Transferring future amenities to a third party

When the seller/developer transfers future amenities to a third party (e.g. a homeowner's association (HOA), municipality or community development district) instead of transferring them to the customer through an undivided interest, it analyzes the transfers differently. Based on discussions with the FASB staff, we believe those third parties generally are not extensions of the customer because they are unrelated to the customer and the customer does not control the amenities before or after the transfer.

While an individual homeowner often has an obligation to pay fees to third-party transferees such as HOA dues or municipal taxes and may have some rights to participate in their operation, such as becoming a board member, appealing fee or tax assessments, or obtaining and reviewing governing documents or financial data, the individual generally does not have an equity interest or the ability to control the third party or the amenity either before or after the transfer. In this situation, the promise associated with the future amenity would not be

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

considered part of the customer's contract to purchase the property because the amenities will be transferred to an unrelated party. Therefore, delivery of the amenity would not be considered a performance obligation in the contract with the customer.

Accounting for amenity costs – amenity transferred to a third party

We believe the guidance on accounting for amenity costs that will be sold separately from the unit applies to these situations because the developer is selling or transferring the future amenity separately to the third party. The amount of capitalizable costs (incurred before the amenity is substantially complete and available for use) that exceeds the estimated fair value at the date of substantial physical completion should be allocated as common costs to the land parcels that benefitted and to those for which development is probable.

Capitalizable costs are reduced by operating income (or are increased by operating losses) generated by the amenity before it is substantially complete and available for use. Operating income (or loss) generated by the amenity after it is substantially complete and available for use is included in operating results. A later sale of the amenity at an amount different from the estimated fair value at substantial completion, less any accumulated depreciation, results in a gain or loss in net income in the period in which the sale occurs. [970-340-25-9(b) – 25-11]

In the scenario described, the third party typically pays little or no consideration on transfer of the amenity. Therefore, we believe that the developer would treat as common costs all the costs associated with the amenity that are not expected to be recovered on transfer to the HOA or municipality.

Question C15

What is the unit of account for noncustomer real estate sales when the disposal group includes more than one asset?

Interpretive response: As discussed in Questions A10 and A20, when a seller transacts with a noncustomer, and substantially all of the fair value of a group's or subsidiary's assets is concentrated in nonfinancial assets and the group or subsidiary is not a business, the seller applies Subtopic 610-20 to the sale of each distinct asset within the group or subsidiary. This includes assets in the entity or group that would be financial assets if they were sold separately but are in-substance nonfinancial assets (as a result of being included in a group or subsidiary in which substantially all the fair value is concentrated in nonfinancial assets). [610-20-15-5 – 15-6]

Each distinct nonfinancial asset (or in-substance nonfinancial asset) is a separate unit of account that needs to be analyzed to determine whether derecognition is appropriate and, if so, the amount of the related gain or loss. Subtopic 610-20 requires the seller to identify each distinct nonfinancial asset using the criteria in Step 2 of the revenue recognition model in Topic 606. [610-20-25-6 – 32-2]

A seller identifies each distinct nonfinancial asset (or in-substance nonfinancial asset) as a separate unit of account even when multiple nonfinancial assets are transferred together in a legal entity. However, the FASB observed that in many

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

cases, control of nonfinancial assets in a subsidiary will transfer at the same time and practically a seller may not need to separately identify the distinct assets when a group or subsidiary has multiple nonfinancial assets and in-substance nonfinancial assets (if any). Nevertheless, a seller should carefully evaluate the arrangement to ensure there are no provisions indicating that assets in a single group or subsidiary will transfer at different times. [ASU 2017-05.BC42]

Also, there may be situations in which the seller retains control of specific assets within the group – e.g. by having a repurchase option on a single asset in the group. In those situations, the seller will need to allocate consideration to each distinct nonfinancial and in-substance nonfinancial asset to compute the gain on those assets for which control has transferred. See Question F60. [610-20-25-6]

Refer to Question 17.3.40 of KPMG Handbook, Revenue recognition, for additional discussion about the unit of account under Subtopic 610-20 and Question F91 for discussion about how the transaction price is allocated when the transaction contains multiple distinct nonfinancial assets.

Question C20

Does the sale of land and the agreement to construct property improvements comprise multiple performance obligations? Is the analysis different if the buyer is not a customer?

Interpretive response:

Contracts with customers

It depends. As discussed in Question C10, a seller accounts for a good or service as a performance obligation only if the good or service promised to the customer is distinct (i.e. capable of being distinct and distinct in the context of the contract) from other goods or services in the contract. [606-10-25-19]

Capable of being distinct

When evaluating whether the transfer of the land and the construction contract are capable of being distinct, the seller/developer considers whether the land alone could be used, consumed, sold for an amount that is greater than scrap value or otherwise held in a way that generates economic benefit. For example, could the land alone be sold, developed by another party or leased to others?

The seller/developer also considers whether the property improvements that are the output of the construction contract could independently generate economic benefits. For example, could the property improvements be sold independently (perhaps if a buyer leased the underlying land) or leased?

The seller/developer also considers whether it (or a similar party) regularly sells land or construction services separately. [606-10-25-20]

We believe a seller/developer often may conclude that the sale of the land and construction service contract are capable of being distinct, but it needs to consider all the facts and circumstances. See Question C10 about how a seller/developer may evaluate this criterion in a property sale with an

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

accompanying undivided interest in common areas where future amenities may be built.

Distinct in the context of the contract

When the seller/developer evaluates whether the sale of the land and the construction contract are distinct in the context of the contract, its objective is to determine whether the nature of its overall promise is to transfer each of the goods or services, or whether the promise is to transfer a combined item to which the promised goods or services are inputs.

Factors that indicate a good or service is **not** distinct in the context of the contract, include, but are not limited to:

- **Indicator a** – the entity provides a significant service of integrating the goods or services with other goods or services promised in the contract;
- **Indicator b** – one or more of the goods or services significantly modifies or customizes, or is significantly modified or customized by, one or more of the other goods or services promised in the contract; or
- **Indicator c** – the goods or services are highly interdependent or highly interrelated (i.e. each one is significantly affected by the other goods or services).

Indicator a

While land appears to be an input to delivering a property improvement, the land with the property improvements may not be the combined output specified in the contract. The land transfer and property improvement construction may be separate promises in the contract.

For example, these contract terms may suggest the promises are separate:

- the stated contract consideration (not necessarily the transaction price) for the land sale may be independent of the construction service consideration;
- the timing for delivery of each promise may be different because the title to the land transfers to the buyer before construction begins; or
- the dispute resolution or default provisions associated with the land sale, the construction contract, or both, do not affect the terms of the other promise.

Indicator b

Whether property improvements significantly modify or customize the land may depend, in part, on the nature of the improvement and the characteristics of the land. For example, certain land parcels may be expected to have largely the same value with or without the property improvements – e.g. one in a unique location and/or zoned for a particular use. Other land parcels may not require significant site preparation (demolition, clearing, grading or excavation) so the construction of the improvements may not significantly modify or customize the land.

Indicator c

This indicator focuses on whether the promises affect each other to such an extent that delivery/satisfaction of one without the other, and vice versa, would significantly affect the value or utility of the delivered/satisfied promise.

The FASB's guidance provides one example of highly interrelated promises when an entity grants a customer an antivirus software license along with

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

when-and-if-available updates. The updates occur frequently and are critical to the continued utility of the software because without them the customer's ability to benefit from the software would decline significantly. These promises are not distinct in the context of the contract because the license and its updates are inputs to a combined output of antivirus protection.

The updates significantly modify the functionality of the software to ensure that it protects the customer from new viruses and are integral to maintaining the software's utility. The license and the updates fulfill a single promise to the customer, which is to provide protection from computer viruses. We believe that the FASB intended this example to illustrate a very narrow fact pattern that is specific to certain software license arrangements. [606-10-55-140D – 55-140F]

The FASB provided another example of an entity contracting with a customer to sell a piece of equipment with installation services that are not complex and are capable of being performed by alternative service providers. In this scenario, the promises are distinct in the context of the contract for the following reasons.

a. The entity is not providing a significant integration service. Instead, the entity has promised to deliver the equipment and install it. The entity would be able to fulfill its promise to transfer the equipment separately from its promise to install it. The entity has not promised to combine the equipment and the installation services in a way that would transform them into a combined output.

b. The installation services will not significantly customize or modify the equipment.

c. Although the customer can benefit from the installation services only after it has obtained control of the equipment, the installation services do not significantly affect the equipment because the entity would be able to fulfill its promise to transfer the equipment independently from its promise to provide installation services. Because the equipment and the installation services do not significantly affect each other, they are not highly interdependent or highly interrelated. [606-10-55-150A – 55-150D]

Even if the customer is contractually required to use the entity's installation services, the promises are still distinct because the contractual requirement does not change the characteristics of the goods or services, nor does it change the entity's promises to the customer. [606-10-55-150E – 55-150F]

When applying this guidance to land sales with accompanying development contracts, we believe sellers/developers often will conclude that the land and construction services are not highly interdependent or highly interrelated because generally a customer could benefit independently from the land and construction services.

For example, a customer could purchase the land and hire another party to perform the construction services and conversely could purchase, lease or redeploy other land on which the developer could construct the improvements. While the contract allows the customer to benefit from the construction services only after it has obtained control of the land, generally the seller/developer can fulfill its promise to transfer the land independently of its promise to perform the construction services.

However, there may be situations in which the land sale and the development contract are highly interdependent or interrelated. This could occur when the

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

entire project is so complex or specialized that the value of the combined output (i.e. the completed property) relies primarily on the seller/developer's proprietary knowledge, skill or position in the market. In these unusual situations, the parties to the contract also likely would conclude that indicator (a) is met because the seller/developer performs a significant service of integrating the land sale and the construction services to deliver a transformed combined output for which the buyer has contracted.

A contractual requirement to use the same seller/developer for the land sale and construction services does not affect the conclusion about whether the promises are distinct. [606-10-55-150E – 55-150F]

Careful consideration of the total contract and all relevant facts and circumstances about the delivery of goods or services to the customer are critical when evaluating whether promises are distinct in the context of the contract.

Contracts with noncustomers

Subtopic 610-20 refers to Topic 606's guidance on separating performance obligations only in the context of the seller identifying the distinct nonfinancial and in-substance nonfinancial assets to which it will allocate the contract consideration. However, it also says that if a contract to sell a nonfinancial (or in-substance nonfinancial) asset includes other promises (e.g. services or guarantees in the scope of Topic 460) that do not relate to assets of the seller to be derecognized, those arrangements are separated and accounted for under other Topics. [610-20-15-9 – 15-10, 25-6]

We believe that if a seller/developer routinely sells land as an output of its ordinary activities, the land sale and construction services likely are both within the scope of Topic 606 on customer transactions. Those sellers would assess the number of performance obligations as discussed above.

If the seller/developer routinely provides construction services as an output of its normal activities but does not routinely sell land as part of those activities, it would apply Subtopic 610-20 to the land sale and Topic 606 to the construction services if those two promises are distinct. We believe the seller generally would allocate the total transaction price between these two units of account using relative stand-alone selling prices. See additional discussion in Question E10. [610-20-15-9 – 15-10, 25-6, 32-2 – 32-6, 606-10-15-4, 32-29]

If the land and construction services are not distinct, the evaluation would be based on whether their combined output (the land sale and services) is an output of the seller/developer's normal activities.

See additional discussion in Question F30 about the timing of revenue recognition for land sales with accompanying construction contracts.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question C30

How should an entity analyze the number of performance obligations in a typical property management services contract?

Interpretive response: The manager first must identify the promises to the customer and evaluate whether each promise is distinct (see the response to Question C20 for the distinct criteria). When evaluating whether the multiple promises are distinct the manager will generally focus on determining whether the nature of the property management services is to provide a single, integrated service offering, and therefore the individual activities that comprise property management are not distinct in the context of the contract.

While each activity conducted by a manager may be capable of being distinct, the activities may not be separately identifiable when the manager provides a significant service of integrating the activities such that they become essentially fulfillment activities or inputs to provide the management service.

A key consideration in this determination is whether the activities the manager will perform to fulfill the performance obligation are indeterminate (e.g. even if the type of activities are generally understood, the quantity and mix of activities that will need to be performed to fulfill the obligation are unknown), or are known upfront – e.g. the manager will do X, Y and Z activity once weekly for three years. A manager with a promise to provide indeterminate activities is likely to conclude that it is providing a single, integrated service offering to the customer – i.e. it is conducting all of the activities to perform a single promise of an outsourced service for the customer.

If the property management services are not a single integrated service offering, the manager should analyze each specified activity to determine if it is distinct from the other activities to conclude on the number of performance obligations.

If the property management services are a single integrated service offering, the manager may still need to determine whether the integrated service is a 'series'. For example, could a three-year property management services contract be subdivided into distinct time periods like three annual periods or 36 monthly periods? This may be important for purposes of allocating variable consideration (see Question E10) or subsequent modifications.

A performance obligation is a series when it comprises distinct goods or services that are substantially the same and have the same pattern of transfer. When the integrated service can be subdivided into smaller time increments during which the manager's promises are substantially the same in each time increment, the performance obligation may be a series if each time increment is distinct.

After subdividing the service period into time increments, the manager must evaluate whether those identified increments are distinct from each other. If so, the manager considers the services a series of distinct services that are accounted for as a single performance obligation (i.e. series guidance in Topic 606). If the time increments are not distinct, the property management services are still a single performance obligation but not a series. See Question E10 for additional discussion. [606-10-25-14 – 25-15, 25-19 – 25-21]

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

The FASB illustrates this guidance in an example where property management services are accounted for as a single performance obligation under the series guidance. [606-10-55-157B – 55-157E, Ex 12A]

The example reaches this conclusion because:

a. Each day's property management services are substantially the same because the manager provides the same overall service each day, even if the underlying tasks or activities vary – e.g. cleaning services, leasing or reservation services, property maintenance;

b. Each day of property management services is satisfied over time because the customer simultaneously receives and consumes the benefits provided by the manager as it performs (see the discussion of the over-time criteria in Question F20); and

c. The same method is used to measure progress toward complete satisfaction of the performance obligation because each day's obligation to provide property management services typically is measured using a time-based approach. [606-10-25-15, 25-27]

For more information see the following Questions:

- D30 – determining the transaction price when the property management services contract accompanies a property sale;
- E10 – allocating the transaction price when the property management services contract accompanies a property sale; and
- F130 – recognizing revenue for variable consideration in a property management services contract.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

D. Step 3: Determine the transaction price

Questions and Examples

Q&A D10 How does a seller's right to participate in a property's future profits affect the determination of the transaction price for the sale of that property?

Example D10.1 Sale of property with future profits interest

Q&A D15 Are incentive fees (e.g. in property or asset management agreements) that are subject to variability due to market prices or volatility always constrained to zero?

Example D15.1 Applying the constraint to an asset management contract when there is market volatility

Q&A D20 Is a change in estimate relative to the measure of progress toward satisfaction of the performance obligation on a construction contract subject to the revenue recognition constraint?

Q&A D30 What discount rate does an entity use when determining the time value of money to include in the transaction price for a property management service contract that is prepaid as part of an all cash operating property sale?

Example D30.1 Sale of property with prepaid property management services

Q&A D40 When a seller receives nonmonetary consideration in a property sale, does it apply the guidance for nonmonetary transactions or the guidance on noncash consideration?

Q&A D45 Does a seller in a real estate sale recognize as noncash consideration the receipt of a real estate option that is outside the scope of Topic 815?

Q&A D50 How does a seller consider liabilities assumed by the buyer in a sale of real estate to a noncustomer?

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question D10

How does a seller's right to participate in a property's future profits affect the determination of the transaction price for the sale of that property?

Interpretive response: The seller generally treats its right to future profits as variable consideration and estimates it upfront to determine the transaction price (the amount of consideration to which it expects to be entitled). The seller would not estimate its right to future profits upfront as part of the transaction price for the property sale if: [606-10-32-40, 55-18]

a. it must allocate the future profits entirely to another performance obligation, or to distinct goods or services within a series of distinct goods or services that are accounted for as a single performance obligation; or

b. the contract also contains another performance obligation satisfied over time and the entity recognizes the future profits as revenue for that performance obligation in the amount to which the entity has a right to invoice as a practical expedient.

Variable consideration included in the transaction price is subject to a constraint and is regularly reassessed until the uncertainty is resolved. A seller may only include its estimate of its share of future profits in the transaction price to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty is subsequently resolved. [606-10-32-11 – 32-14]

The guidance on the constraint requires a seller to consider both the likelihood and the magnitude of a potential revenue reversal and includes the following factors that could increase the likelihood or the magnitude of a revenue reversal. [606-10-32-12]

- The amount of consideration is highly susceptible to factors outside the seller's influence. Those factors may include market volatility, the judgment or actions of third parties, weather conditions, and a high risk of obsolescence of the promised good or service.
- The seller does not expect resolution to the uncertainty about the amount of consideration for a long time.
- The seller's experience or other evidence with similar contracts is limited, or that experience or other evidence has limited predictive value.
- The entity has a practice of either offering a broad range of price concessions or changing the payment terms and conditions of similar contracts in similar circumstances.
- The contract has a large number and broad range of possible consideration amounts.

The seller must estimate the transaction price in light of the specific facts and circumstances of the arrangement and cannot default to a conclusion that the variable consideration is fully constrained until the uncertainty is resolved. The seller will update the estimated transaction price each reporting period to reflect the current circumstances at each reporting date.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

The guidance on determining the transaction price applies to both customer and noncustomer transactions.

Example D10.1

Sale of property with future profits interest

Description of the arrangement

ABC Corp. sells a newly constructed retail property with a cost of $1,200,000 to DEF Corp. for $2,000,000 in cash and a right to receive 5% of future operating profits from the property over a 10-year earn-out period. ABC has no ongoing performance obligations related to the operations of the property.

Because the in-place leases have fixed payments for the first two years of the earn-out period, ABC concludes it is probable that it will receive a payout of $50,000 in total variable consideration for years one and two. It bases its belief on the contractual, fixed lease payments in those years and its experience with similar properties and tenants.

However, ABC is less certain about its expected payouts in years 3 through 10 because the lease payments that the property buyer will receive shift from fixed payments to contingent payments based on the lessees' underlying third-party sales. While ABC is not guaranteed a minimum payout in years 3-10 and there is more uncertainty than the payouts expected in years one and two, it nevertheless can estimate its expected payout based on its experience with similar properties and tenants.

ABC estimates it will be entitled to at least $250,000 in earn-out payments in years 3-10 and concludes it is probable that a significant reversal of the variable consideration when compared to cumulative revenue of $2,300,000 will not occur. The transaction price amount is the contractual selling price of $2,000,000 plus $300,000 of the variable consideration for the 10-year earn-out period. ABC does not believe it has a basis to reasonably estimate any additional earn-out amounts because of its level of uncertainty about receipts in excess of $300,000.

Evaluation

Gain of $1,100,000 ($2,000,000 contractual selling price + $300,000[9] in variable consideration – $1,200,000 cost) is recognized when control of the property transfers. The $300,000 of variable consideration is included in the transaction price because it is probable a significant reversal compared to the cumulative revenue recognized of $2,300,000 will not occur.

ABC continually assesses the variable consideration, considering the constraint, and revises its estimates accordingly.

---

9 The effect of the time value of money is not analyzed when consideration is variable and its timing varies based on the occurrence or nonoccurrence of a future event that is not substantially within the control of the customer or entity. [606-10-32-17(b)]

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question D15

Are incentive fees (e.g. in property or asset management agreements) that are subject to variability due to market prices or volatility always constrained to zero?

Interpretive response: No. As discussed in Question D10, a contract with variable consideration based on market prices or subject to volatility does not necessarily mean the transaction price should be fully constrained. In certain circumstances, it may be appropriate to include variable amounts in the transaction price even if the realization of the variable consideration continues to be subject to market prices or volatility.

Although consideration being highly susceptible to factors outside an entity's influence is a factor that suggests an increased likelihood or magnitude of a revenue reversal, that factor is not determinative in concluding whether variable consideration could be recognized. [606-10-32-12]

Therefore, depending on an entity's evaluation of these factors, circumstances may exist in which an entity concludes that it is able to recognize some amount of revenue even when fees vary due to factors outside its control. An entity would need appropriate evidence to support that its estimate of the transaction price reflects the application of the constraint.

Example D15.1

Applying the constraint to an asset management contract when there is market volatility[10]

Asset Manager enters into a two-year contract to provide asset management services to Fund, a non-registered investment partnership. Fund's objective is to invest in real estate properties. In addition to a fixed management fee, Asset Manager earns a performance-based incentive fee equal to 20% of Fund's return in excess of an established hurdle rate over the contract period.

Asset Manager determines that the contract includes a single performance obligation (series of distinct services) that is satisfied over time and identifies that the performance fee is variable consideration. Before including the estimates of the performance fee in the transaction price, Asset Manager considers whether the constraint applies to the performance fee.

Contract inception

At contract inception, Asset Manager determines that the cumulative amount of consideration is constrained because the promised consideration for the performance fee is highly susceptible to factors outside its own influence.

10 This example is adapted from Example 25 in Topic 606.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Subsequent reassessment

At each subsequent reporting date, Asset Manager concludes the full amount of the performance fee is constrained, and therefore excluded from the transaction price. This is because:

- the performance fee has a high variability of possible consideration amounts, and the magnitude of any downward adjustment could be significant;
- although Asset Manager has experience with similar contracts, that experience is not predictive of the outcome of the current contract; this is because the amount of consideration is highly susceptible to volatility in the market (based on the nature of the assets under management); and
- there are a large number of possible outcomes.

This determination is made each reporting date and could change toward the end of the contract period.

Assume that with three months left, Fund has achieved an annualized rate of return significantly in excess of the hurdle rate and, as such, Asset Manager liquidates the remainder of the investments and invests the cash into a money market fund for the remainder of the contract term. Based on the annualized rate of return achieved to date compared to the hurdle rate, Asset Manager concludes that a subsequent significant reversal in relation to cumulative revenue recognized is not probable for the entire incentive fee given the risk of not achieving the rate of return has been mitigated by investing the Fund's assets in low-risk money market funds.

At that point, Asset Manager would include at least some of the estimated variable consideration in the transaction price.

Question D20

Is a change in estimate relative to the measure of progress toward satisfaction of the performance obligation on a construction contract subject to the revenue recognition constraint?

Interpretive response: The objective of the constraint on variable consideration is to recognize revenue only to the extent it is probable the cumulative amount of revenue recognized is not subject to a risk of significant revenue reversal **due to variability in the transaction price**. While a construction contractor may experience revenue reversals when it changes its estimate of progress toward complete satisfaction of a performance obligation, these reversals do not represent changes in the ultimate consideration to which the developer is entitled. [606-10-32-11 – 32-14]

The risk associated with a change in timing of total revenue is not evaluated under the constraint. However, significant changes in timing may:

a. call into question the contractor's ability to reasonably estimate its progress;
b. result in a reassessment of whether performance bonuses or penalties in the contract may occur, which would affect the transaction price; and

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

c. suggest that the contractor should evaluate the need to recognize a provision for anticipated losses on the contract. [606-10-25-36 – 25-37, 605-35-25-45 – 25-49]

Question D30

What discount rate does an entity use when determining the time value of money to include in the transaction price for a property management service contract that is prepaid as part of an all cash operating property sale?

Interpretive response: This question assumes that the property sale and the property management service contract[11] are two performance obligations or units of account.[12]

The objective when adjusting the promised amount of consideration for a significant financing component is for an entity to recognize revenue at an amount that reflects the price the customer would have paid if it had paid cash for the promised goods or services when or as control transfers. Therefore, a seller determines the discount rate by identifying the rate that would discount the stand-alone selling price (and related timing) of the property management services to the allocated transaction price. [606-10-32-15, 32-20]

The discount rate should be the rate that would exist in a separate financing transaction between the buyer and the seller at contract inception that reflects the credit characteristics of the party receiving financing in the contract, and collateral or security provided by the buyer or the seller, if any, including assets transferred in the contract.

The seller adjusts the transaction price to reflect the time value of money only if the financing component is significant to the **contract**, not necessarily significant to one or more of the separate performance obligations. In this case, the seller would evaluate the significance of the financing component associated with the prepayment of the property management services relative to the transaction price of the contract (i.e. the transaction price for the sale of the property and property management services combined).

A contract does not have a significant financing component even if the timing of payments and the transfer of control of the goods or services differs significantly if one of these factors exist:

---

[11] The property management services are determined to be a single performance obligation because the entity is providing a series of distinct services that are substantially the same with the same pattern of transfer. See additional discussion in Question C30. [606-10-25-14(b)]

[12] If selling land and providing property management services are both an output of the entity's ordinary activities, the entity evaluates whether it has one or more performance obligations under Topic 606. If not, the seller may have two units of account – e.g. it applies Subtopic 610-20 to the sale of the land to a noncustomer and Topic 606 to the property management services provided to a customer. See Question C20.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

- the customer makes an advance payment, and the timing of the transfer of goods or services is at the customer's discretion;
- a substantial amount of the consideration is contingent on a future event outside the parties' control; or
- the difference between the promised consideration and the cash-selling price arises for reasons other than financing. [606-10-32-17]

As a practical expedient, a seller does not need to account for a financing component when the period is expected to be one year or less between when the seller transfers a good or service and when the customer pays for the good or service. [606-10-32-18]

The guidance on determining the transaction price applies to both customer and noncustomer transactions.

Example D30.1

Sale of property with prepaid property management services

Description of the arrangement

ABC Corp. sells an office building with a carrying amount of $1,500,000 and agrees to manage the office building for three years. ABC routinely provides property management services as an output of its normal activities but does not typically sell property.

The buyer pays $2,000,000 in cash at the date of sale for the office building and the management services. ABC identifies two units of account ((1) sale of office building to a noncustomer and (2) property management services provided to a customer) and allocates $1,714,286 of the transaction price to the sale of the office building and $285,714 to the future property management services (see Example E10.1 for illustration).

ABC makes these allocations based on the stand-alone selling prices of $1,800,000 for the office building and $300,000, or $100,000 per year, for the property management services. ABC determines that the financing component is significant to the contract, and that the property management services will be delivered evenly over the three-year service period.

Evaluation

Because ABC has determined that the financing component is significant to the contract, it establishes an initial contract liability of $285,714 and accrues interest expense each period on that liability. ABC calculates the interest rate by determining what rate discounts the cash selling price of the property management services ($300,000 or $100,000 per year for 3 years of monthly payments) to the promised consideration (i.e. $285,714).

The interest rate implicit in the contract is 3.19%, which ABC concludes is reasonable relative to what its borrowing rate would be in a separate financing transaction. This rate (and the resulting interest expense amounts below) assume monthly payments on the contract liability equal to $8,333.33 ($300,000 over 36 months) to reflect the property management services being delivered evenly over time.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

One way to account for this would be as follows.

At inception

	Debit	Credit
Cash	285,714[(1)]	
Contract liability		285,714
To reflect cash received that is allocated to property management services.		
Cash	1,714,286[(2)]	
Property and equipment		1,500,000
Gain		214,286
To record gain on sale of office building.		
Note: 1. (1) + (2) = $2,000,000 cash consideration received from buyer.		

Year 1

	Debit	Credit
Interest expense	7,783	
Contract liability		7,783
To accrue aggregate annual interest expense (based on hypothetical monthly payments) on contract liability.		
Contract liability	100,000	
Revenue		100,000
To recognize Year 1 property management service revenue.		

Year 2

	Debit	Credit
Interest expense	4,794	
Contract liability		4,794
To accrue aggregate annual interest expense (based on hypothetical monthly payments) on contract liability.		
Contract liability	100,000	
Revenue		100,000
To recognize Year 2 property management service revenue.		

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Year 3

	Debit	Credit
Interest expense	1,709	
Contract liability		1,709
To accrue aggregate annual interest expense (based on hypothetical monthly payments) on contract liability.		
Contract liability	100,000	
Revenue		100,000
To recognize Year 3 property management service revenue.		

Question D40

When a seller receives nonmonetary consideration in a property sale, does it apply the guidance for nonmonetary transactions or the guidance on noncash consideration?

Interpretive response: Topic 606 and Subtopic 610-20 supersede most of the real estate-specific exchange guidance in Topic 845 (nonmonetary transactions). However, Topic 845 still applies to nonmonetary exchanges between entities in the same line of business to facilitate sales to customers or potential customers (e.g. exchanges of similar land lots between real estate developers) because Topic 606 excludes those transactions. [606-10-15-2(e)]

When Topic 845 is applicable

A nonmonetary exchange shall be measured based on the recorded amount (including any impairment) of the nonmonetary asset(s) relinquished, and not the fair value of the exchanged assets. No gain or loss is recognized. [845-10-30-3]

When Topic 606 is applicable

When the consideration received in a sale of real estate includes noncash consideration, the seller/transferor measures the noncash consideration at fair value. If the seller cannot make a reasonable estimate of the fair value of the noncash consideration, it uses the stand-alone selling price of the promised goods or services. [606-10-32-21 – 32-22, 610-20-32-4]

The seller measures the noncash consideration at contract inception – i.e. the date at which the conditions are met to conclude a contract exists. [606-10-32-21, 606-10-25-1 – 25-8]

Changes in the fair value of the consideration after contract inception are: [606-10-32-23]

— not included in the transaction price if they are due to the form of the consideration – e.g. changes in the share price of securities or changes in the fair value of nonfinancial assets which the entity is entitled to receive from a customer; or

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

- variable consideration if they are caused by something other than the form of the consideration – e.g. the exercise price of a share option changes because of the entity's performance.

If the changes in the fair value of the consideration are due to both the form of the consideration and some reason other than the form of the consideration, then the seller applies the variable consideration guidance only to the variability resulting from reasons other than the form of the consideration.

This guidance applies to all transactions in the scope of Subtopic 610-20, which includes traditional partial sale transactions, contributions to form real estate joint ventures (assuming the seller retains only a noncontrolling interest), and transfers of nonfinancial assets to an existing equity method investee. Noncash consideration also includes receipt of a new or incremental noncontrolling interest in the entity that owns the asset post-sale. Because the seller measures the noncash consideration received in the form of a retained noncontrolling interest at fair value in these transactions, it will recognize 100% gain when control of the nonfinancial (or in-substance nonfinancial) asset transfers to the noncontrolled buyer. [610-20-05-2, 32-2 – 32-4]

For information about control transfer when a noncontrolling interest is retained or received, see Question F90. Refer to Question 17.2.40 of KPMG Handbook, Revenue recognition, for additional discussion about transfers of nonfinancial assets for nonmonetary consideration and Question 17.3.80 of the Handbook for discussion about the receipt of a noncontrolling interest in a counterparty as noncash consideration.

Question D45

Does a seller in a real estate sale recognize as noncash consideration the receipt of a real estate option that is outside the scope of Topic 815?

Interpretive response: Yes. As discussed in Question D40, when the consideration received in a sale of real estate includes noncash consideration, the seller/transferor generally measures the noncash consideration at fair value. We believe this guidance applies when a seller receives an option to purchase real estate that is not subject to the sale, regardless of whether the option is a derivative within the scope of Topic 815. The seller will then apply the subsequent measurement guidance in Topic 815 only if the option is within its scope. [606-10-32-21 – 32-22, 610-20-32-4]

A seller applies the guidance on noncash consideration when it concludes that it has a contract with the buyer. However, if the seller receives an option to repurchase the property subject to the sale, the option generally prevents control transfer to the buyer. For information about the effects of repurchase rights on sale accounting, see Question F70.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question D50

How does a seller consider liabilities assumed by the buyer in a sale of real estate to a noncustomer?

Interpretive response: Under Subtopic 610-20, when a contract exists and the seller transfers control of the property, the seller derecognizes the real estate and recognizes a gain or loss equal to the difference between the amount of consideration received and the carrying amount of the real estate. The amount of consideration that is included in the calculation of the gain or loss includes both the *transaction price* and the carrying amount of liabilities assumed or relieved by the buyer. [606-10-32-3, 610-20-32-2 – 32-5]

If control of the real estate transfers before the liability is extinguished under Topic 405 (liabilities) and therefore the liability cannot be derecognized at the same time as the real estate, the seller applies the guidance on constraining estimates of variable consideration to determine the carrying amount of the liability to include in the gain or loss calculation. For example, if the debt was issued at a premium and that premium is expected to decline through amortization between the time control of the asset transfers and the time the debt is extinguished, the seller should estimate the carrying amount of the debt as of the date it is expected to be extinguished for purposes of determining the gain or loss on the sale of the real estate. The seller then recognizes this amount as a contract asset, which represents the consideration it has not yet received in exchange for transferring the assets. [610-20-32-5, 45-3, 405-20-40-1, 606-10-32-11]

If control of the real estate transfers after the liability is extinguished (and therefore the real estate cannot be derecognized at the same time as the liability), the seller derecognizes the liability and recognizes the amount as a contract liability, which represents the consideration received before transferring control of the asset. [610-20-45-3]

Refer to Question 17.3.60 of KPMG Handbook, Revenue recognition, for discussion on what to consider when determining the transaction price and how the amount of consideration is used to calculate the gain or loss. Refer to Question 17.3.70 of the Handbook for discussion about how the amount of liability assumed or relieved by the counterparty is included in the consideration received.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

E. Step 4: Allocate the transaction price

Question and Example

Q&A E10 How does the seller allocate the transaction price in a contract that transfers control of a property and also requires the seller to provide ongoing property management services to a customer? What if the buyer is not a customer?

Example E10.1: Sale of property with ongoing property management services

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question E10

How does the seller allocate the transaction price in a contract that transfers control of a property and also requires the seller to provide ongoing property management services to a customer? What if the buyer is not a customer?

Interpretive response:

Sale of property to a customer

When the sale of the property and the property management services[13] are separate performance obligations, the seller generally allocates the transaction price based on relative stand-alone selling prices – i.e. the price at which an entity would sell a promised good or service separately to a customer. However, in some cases the seller attributes variable consideration and discounts to some, but not all, performance obligations or distinct goods and services within a series of distinct goods or services that comprise a single performance obligation under paragraph 606-10-25-14(b). [606-10-25-15, 32-36 – 32-40]

The seller should first consider the guidance on allocating variable consideration. If the contract includes consideration that is variable, the seller will need to determine if the variable consideration should be allocated to one or both performance obligations. The seller must allocate variable consideration (and subsequent changes to that amount) entirely to a single performance obligation (or to distinct goods or services within a series of distinct goods or services that are accounted for as a single performance obligation) if the:

a. terms of the variable payment relate specifically to the entity's efforts to satisfy the performance obligation or the distinct good or service within the series, and

b. allocation of the variable amount entirely to the performance obligation or the distinct good or service within the series is consistent with the objective to allocate the transaction price in an amount that depicts the consideration that the entity expects to be entitled to in exchange for the promised goods or services after considering the contract's performance obligations and payment terms. [606-10-32-28, 32-40]

It is common for stand-alone property management service contracts to include a base fee and a variable fee that may depend on the property's operations, the manager's cost to provide certain services, or both. A real estate sale with an accompanying property management services contract also may include variable consideration. The seller/property manager needs to consider the guidance on allocating variable consideration when concluding whether it should allocate the variable component entirely to the property management services or to both the property management services and the property sale. [606-10-32-40]

---

[13] See Question C30 on accounting for a series of distinct, daily property management services as a single performance obligation.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

If the seller allocates the variable consideration entirely to the property management services, it will need to determine if those services constitute a series of distinct time increments of property management services. If the seller concludes the property management services are a series of distinct time increments of services (i.e. a series of daily, weekly, monthly management services), it must further allocate the variable consideration to the distinct service periods within the single series performance obligation if the:

a. variable consideration earned for a given distinct service period relates specifically to the seller's services for that period (or an outcome from those services), and
b. allocation of that amount specifically to the distinct service period is consistent with the allocation objective. [606-10-32-28, 32-40]

The seller follows these steps to determine whether to allocate variable consideration to distinct service periods within the single performance obligation:

— First, the seller must determine whether the nature of the property management services is to provide a single, integrated service offering for a defined period of time, or to perform a specified set of activities during the period. Important to this determination is whether the activities the seller will perform to fulfill the performance obligation are indeterminate (e.g. even if the type of activities is generally understood, the quantity and mix of activities that will need to be performed to fulfill the obligation are unknown), or are known upfront (e.g. the seller will do X, Y and Z once each week for three years). If the activities are indeterminate then the performance obligation generally consists of distinct service periods.

— Second, the seller must determine whether the nature of the promise is substantially the same in each time increment. For example, could a three-year property management services contract be subdivided into time periods like three annual periods or 36 monthly periods?

— Third, the seller must determine whether the time increments of service are distinct from each other. If they are not distinct, then the series guidance cannot apply to the property management services performance obligation.

— Finally, if there is a series of distinct service periods within the single property management services performance obligation, the seller must determine whether the fees relate specifically to the seller's efforts to transfer the distinct services (or an outcome from those services) and allocating the variable fees earned during each distinct service period only to that service period is consistent with the allocation objective. [606-10-25-19 – 25-21, 32-40]

If the seller must allocate the variable consideration entirely to the property management services performance obligation, **and** that performance obligation is a series of distinct service periods to which the variable consideration earned each period can be allocated, the seller may not need to estimate the total variable fees that will be earned during the contract to account for the performance obligation. The variable fees earned each period will be allocated to, and recognized in, each period.

If the seller (a) cannot allocate the variable consideration entirely to the property management services performance obligation, (b) the obligation is not a series

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

of distinct service periods or (c) the variable consideration earned each distinct service period within a series cannot be allocated to that distinct service period, the seller generally will need to estimate the total transaction price associated with that performance obligation (including the variable consideration) to which the seller expects to be entitled for performing the property management services over the full performance obligation service period subject to the constraint. The constraint limits the seller to only including estimates of variable consideration in the transaction price to the extent that it is probable that a significant reversal in the cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved. See additional discussion about the constraint in Questions D10 and D15. [606-10-32-11 – 32-14]

The seller will recognize the transaction price (which may include fixed and variable consideration) allocated to the property management services over time based on an appropriate measure of progress as the performance obligation is satisfied. For additional discussion about recognizing property management service revenue, see Questions D15 and F130.

If the sale and accompanying property management services contract also include a future profits interest (see Question D10), the seller would perform a similar analysis because of the variable consideration and existence of more than one performance obligation.

After the seller allocates variable consideration, it will need to determine if any discount should be allocated entirely to one of the performance obligations or allocated proportionately. The discount is the difference between the transaction price and the sum of the stand-alone selling prices. The guidance on the allocation of variable consideration discussed above differs from the guidance on the allocation of a discount to some, but not all, performance obligations or to distinct goods or services within a series of distinct goods or services that are accounted for as a single performance obligation. An entity should allocate a discount entirely to one or more, but not all, of the performance obligations if all of the following conditions exist:

— the entity regularly sells each distinct good or service (or each bundle of distinct goods or services) in the contract on a stand-alone basis;

— the entity also regularly sells on a stand-alone basis a bundle (or bundles) of some of those distinct goods or services at a discount to the stand-alone selling prices of the goods or services in each bundle; and

— the discount attributable to each bundle of goods or services described is substantially the same as the discount in the contract, and an analysis of the goods or services in each bundle provides observable evidence of the performance obligation to which the discount in the contract belongs. [606-10-32-37]

In our experience, most real estate companies do not offer a wide range of bundled goods or services. Therefore, in most cases, these conditions will not exist, and the seller will allocate the discount to all performance obligations in the contract on a relative stand-alone selling price basis. See Example E10.1.

Sale of property to a noncustomer

As discussed in Questions D30 and C20, if selling property and providing property management services are both an output of the seller's ordinary

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

activities, the seller evaluates whether it has one or more performance obligations under Topic 606. If it has more than one performance obligation, the seller allocates the transaction price as discussed above.

If the seller routinely provides property management services as an output of its normal activities, but does not routinely sell property as part of those activities, it would apply the guidance in Subtopic 610-20 to the property sale and Topic 606 to the property management services. We believe the seller generally would allocate the total transaction price between the two units of account using the same guidance described above for sales of property to customers. After the seller allocates the total transaction price to the Subtopic 610-20 promise and the Topic 606 promise, it may need to further allocate those individual transaction prices to multiple performance obligations (within the Topic 606 promise) and multiple distinct assets (within the Subtopic 610-20 promise). [610-20-15-9 – 15-10, 25-6, 32-2 – 32-6]

Example E10.1
Sale of property with ongoing property management services

Description of the arrangement

ABC Corp. sells an office building with a carrying amount of $1,500,000 and agrees to manage the office building for three years for total consideration of $2,000,000 payable in cash upon closing of the sale.

ABC routinely provides property management services as an output of its normal activities but does not typically sell property.

The estimated stand-alone selling price of the office building and the series of management services are $1,800,000 and $300,000, or $100,000 per year, respectively. Assume that the:

a. customer makes no ongoing payments for the services;
b. financing component is not significant to the contract;[14] and
c. criteria for allocating the overall discount entirely to one of the performance obligations are not met. [606-10-32-37]

Evaluation

The seller allocates the total transaction price of $2,000,000 to the two separate units of account based on relative stand-alone selling prices.

Combined stand-alone selling price: $2,100,000
$1,800,000 (property stand-alone selling price) + $300,000 (property management services stand-alone selling price at $100,000 each year for 3 years)
Transaction price allocated to property sale: $1,714,286
($1,800,000 ÷ $2,100,000) × $2,000,000

[14] See Example D30.1 for an illustration of the accounting if the financing component is significant to the contract.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Transaction price allocated to property management services[15]: $285,714 ($300,000 ÷ $2,100,000) × $2,000,000
Gain – recognized when control of the property is transferred: $214,286 $1,714,286 – $1,500,000
Property management service fee revenue – recognized over the three-year service period as the performance obligation is satisfied: $285,714

If the arrangement also included ongoing payments of $10,000 per year for the property management services, the process for allocating the total transaction price of $2,030,000 ($2,000,000 payable at closing + $30,000 in ongoing payments of $10,000 per year for three years) would follow the same approach as illustrated above. This approach also assumes that the financing component is not significant to the contract and the discount is not allocated entirely to one unit of account.

The seller would allocate the total transaction price of $2,030,000 to the two units of account based on relative stand-alone selling prices:

Combined stand-alone selling price: $2,100,000 $1,800,000 (property stand-alone selling price) + $300,000 (property management services stand-alone selling price of $100,000 each year for 3 years)
Transaction price allocated to property sale: $1,740,000 ($1,800,000 ÷ $2,100,000) × $2,030,000
Transaction price allocated to property management services: $290,000 ($300,000 ÷ $2,100,000) × $2,030,000
Gain – recognized when control of the property is transferred: $240,000 $1,740,000 – $1,500,000
Property management service fee revenue – recognized over the three-year service period as the performance obligation is satisfied: $290,000

15 The property management services are a single performance obligation because the entity is providing a series of distinct services that is substantially the same with the same pattern of transfer. See further discussion in Question C30. [606-10-25-14(b)]

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

F. Step 5: Recognize revenue

Questions and Examples

Q&A F10 At what point does control typically transfer in a real estate sale when the performance obligation is only delivery of the property?

Q&A F20 When does control typically transfer in a real estate construction contract (e.g. for the development of property improvements such as a building) when the contract represents a single performance obligation for the construction services?

Q&A F25 Does an entity have an enforceable right to payment if the contract does not explicitly state the right to payment on contract termination?

Q&A F30 When does control typically transfer in a contract that includes a property sale and an accompanying construction contract (e.g. for the development of property improvements for the customer, such as a building on the land)?

Example F30.1: Sale of land with construction contract

Q&A F40 Can the seller/developer of a condominium unit (or similar structure) recognize revenue over time as construction of the unit progresses if title to the completed unit does not transfer until construction is completed?

Example F40.1: Sale of a condominium unit

Q&A F50 When does control transfer in a standstill arrangement in which a real estate subsidiary defaults on nonrecourse debt but the lender chooses to maintain the legal relationship until the lender can find a buyer?

Q&A F60 Has control transferred if in connection with the sale of real estate, the seller provides the buyer with an option to put the property back to the seller?

Q&A F70 Has control transferred if in connection with the sale of real estate, the seller obtains the right (or has an obligation) to repurchase the property?

Q&A F80 Is a right of first refusal (or a right of first offer) considered an obligation or right to repurchase the property?

Q&A F90 How should a seller evaluate transfer of control under Subtopic 610-20 when it transfers ownership interests in a legal entity (e.g. in a partial sale) or otherwise retains an interest in the asset (e.g. in a sale to an equity method investee)?

Example F90.1: Partial sale with a retained controlling financial interest

Example F90.2: Partial sale with a retained noncontrolling interest

Example F90.3: Sale to an existing equity method investee

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Q&A F91 How is the transaction price allocated when the transaction contains multiple distinct nonfinancial assets?

Q&A F95 How is the gain or loss on the sale presented in the income statement?

Q&A F100 Does the guidance in Question F90 apply when the venture owns operating real estate that meets the definition of a business?

Q&A F110 Is a buy-sell clause allowing either investor to make an offer to acquire the other's interest in an entity that holds real estate considered an obligation or a right to repurchase the property from the perspective of the investor that sold the real estate to the entity?

Q&A F120 What is the accounting consequence when a general partner in a limited partnership sells a property to the partnership for cash (contributed by the limited partners) and a significant receivable?

Q&A F130 How should a manager recognize revenue associated with variable consideration in a property management services contract when the contract bases the variable consideration on a percentage of the property's operating results?

Example F130.1: Multiple variable payments in one contract allocated to the period they were earned

Q&A F140 When should a real estate broker that is acting as an agent recognize revenue?

Example F140.1: Real estate broker commissions

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question F10

At what point does control typically transfer in a real estate sale when the performance obligation is only delivery of the property?

Interpretive response: An entity recognizes revenue or gain when it transfers control of the property to the buyer. The buyer obtains control of the asset when it has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. A seller must determine at contract inception whether it satisfies the performance obligation over time or at a point in time. If the seller does not satisfy a performance obligation over time, the performance obligation is satisfied at a point in time. A performance obligation to deliver a single asset (or group of assets) on a single settlement date is typically satisfied at a point in time because it does not meet any of the over-time control transfer criteria and there is no progress to measure. [606-10-25-23 – 25-24, 25-27, 610-20-25-1, 25-5 – 25-7]

For performance obligations satisfied at a point in time, these indicators suggest that control has transferred the:

- seller has a present right to payment for the asset;
- buyer has legal title to the asset;
- seller has transferred physical possession of the asset;
- buyer has the significant risks and rewards of ownership of the asset; and
- buyer has accepted the asset. [606-10-25-30]

We believe in the context of US property sales that the guidance generally suggests that control transfers at closing because the closing date is the point in time when most of the indicators typically are met. The Board reached a view consistent with this when it addressed the issue of control transfer in real estate transactions within the scope of ASU 2011-10 (derecognition of in-substance real estate).

Excerpt from ASU 2011-10

BC10. Therefore, an entity would look to the definition and indicators of control in the proposed revenue recognition guidance to determine when the counterparty to the transaction obtains control of the asset (that is, real estate) and when to derecognize the real estate. Under the proposed revenue recognition guidance, indicators that the customer has obtained control of a good or service include, among others, the fact that the customer has legal title and physical possession.

While transfer of control for sales of existing property often occurs at closing, the seller needs to consider the facts and circumstances of the particular transaction. For example, Question B10 illustrates a situation in which the seller transferred legal title and physical possession of the building to the buyer at closing but may have retained control of the building based on its analysis of the control indicators (in addition to failing the requirements to establish contract existence). Questions F50 and F70 address other

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

situations where control may not reside with the party with legal title and physical possession.

The guidance on control transfer applies to both customer and noncustomer transactions; however, additional considerations apply when nonfinancial and in-substance nonfinancial assets are transferred within a legal entity. See Question F90.

Question F20

When does control typically transfer in a real estate construction contract (e.g. for the development of property improvements such as a building) when the contract represents a single performance obligation for the construction services?

Interpretive response: An entity recognizes revenue when it satisfies a performance obligation by transferring control of the good or service to the customer. An entity considers an asset or service transferred when, or as, the customer obtains control of the asset. An entity determines at contract inception whether it satisfies the performance obligation over time or at a point in time. If an entity does not satisfy a performance obligation over time, the performance obligation is satisfied at a point in time. [606-10-25-23 – 25-24]

An entity transfers control of a good or service over time if the transaction meets at least one of the following criteria: [606-10-25-27]

a. The customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs;

This criterion primarily applies to traditional service contracts (e.g. property management services) when the customer is benefitting on a periodic basis as the entity performs (e.g. as the property is being managed) as opposed to service contracts when an asset is being constructed or enhanced on the customer's behalf. When a customer's asset is being constructed or enhanced, further analysis is necessary under criterion (b) and criterion (c) if criterion (b) is not met.

b. The entity's performance creates or enhances an asset (e.g. work in process) that the customer controls as the asset is created or enhanced; or

We believe this criterion generally will be met in a real estate construction contract when the customer owns the underlying land and takes control of the property improvements as construction progresses. In that case, the customer generally is able to direct the use of, and obtain substantially all of the remaining benefits from, the improvements during construction.

The customer generally is able to use the property improvements to enhance the value of other assets during the construction period. The ability to use the property improvements includes selling the land the customer owns on which the improvements are built; selling or exchanging the property, including the partially completed improvements; and pledging the property with the partially completed improvements to secure a loan.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

This analysis applies when the customer controls and holds legal title to the land on which improvements are constructed. A similar analysis also may apply if the customer leases the underlying land on a long-term basis and will own the property improvements. A developer will not meet criterion (b) however, if it (as opposed to the customer) controls the property and/or the improvements until construction is complete. This may occur in constructing condominium units (or similar structures). See Question F40 for additional discussion.

c. The entity's performance does not create an asset with an alternative use to the entity, and the entity has an enforceable right to payment for performance completed to date.

An entity only needs to meet one of the three criteria to conclude that a performance obligation is satisfied over time. We believe this criterion may also be met in a real estate construction contract if the customer owns the underlying land and takes control of the property improvements as construction progresses because the developer's performance generally does not create an asset with alternative use to the developer. Usually the customer controls the property improvements being constructed and those improvements are affixed to land controlled by the customer. Therefore, the developer likely is legally and practically prohibited from directing the improvements for any other use. [606-10-25-27 – 25-28]

However, to meet this criterion, the developer also must have an enforceable right to payment for performance completed to date, which often is the case when a contract includes payment provisions that protect the developer in the event of a termination for convenience by the customer.

When a contract does not specify whether the entity has a right to payment on contract termination, we believe an enforceable right to payment is presumed not to exist. See Question F25 for additional discussion.

If the entity meets at least one of the above criteria, revenue on the construction services performance obligation is recognized over time as satisfaction of the performance obligation progresses. [606-10-25-27]

The guidance on control transfer applies to both customer and noncustomer transactions.

Question F25

Does an entity have an enforceable right to payment if the contract does not explicitly state the right to payment on contract termination?

Interpretive response: Generally, no. We believe that when a contract's written terms do not specify the entity's right to payment upon contract termination, an enforceable right to payment is presumed not to exist. This is consistent with the FASB staff views discussed at the June 26, 2018 Private Company Council meeting. [PCC Memo June 26, 2018]

We believe this presumption (that an enforceable right to payment does not exist) also applies to non-cancellable contracts when there are no written terms to specify the entity's right to payment if the customer breaches the contract.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

However, if the entity asserts that it has an enforceable right to payment for performance completed to date in these circumstances, to overcome this presumption, we would expect it to take the following steps.

— Support its assertion (that it has an enforceable right to payment) based on legislation, administrative practice or legal precedent that confers upon the entity a right to payment for performance completed to date. This analysis should demonstrate that an enforceable right to payment exists in the relevant jurisdiction. [606-10-55-14(a)]

— Assess whether relevant legal precedent indicates that similar rights to payment for performance completed to date in similar contracts have no binding legal effect. [606-10-55-14(b)]

The fact that the entity may have a basis for making a claim against the counterparty in a court of law would not on its own be sufficient to support that an enforceable right to payment exists as discussed in Question 7.3.80 in KPMG Handbook, Revenue recognition.

Question F30

When does control typically transfer in a contract that includes a property sale and an accompanying construction contract (e.g. for the development of property improvements for the customer, such as a building on the land)?

Interpretive response: As discussed in Question C20, a seller/developer first needs to determine whether the contract contains one or more performance obligations or units of account.

In the more common scenario when the property sale and the construction services are two performance obligations or units of account, the seller/developer usually allocates the transaction price to those two performance obligations or units of account based on relative stand-alone selling prices (see Question E10). The seller/developer evaluates each performance obligation or unit of account to determine whether it recognizes revenue or gain over time or at a point in time. As discussed in Question F10, control of property often transfers at a point in time, and as discussed in Question F20, construction services (as a stand-alone performance obligation or unit of account) are often, but not always, satisfied over time.

In the less common scenario when the property sale and the construction contract comprise a single performance obligation or unit of account, the entity will need to analyze whether the single performance obligation or unit of account is satisfied:

— at a point in time – upon delivery of the completed property, including improvements; or
— over time – as title to the land transfers and construction progresses on the improvements affixed to the buyer-owned land.

If title to the land transfers to the buyer before construction begins, and the buyer owns the improvements during construction, we believe the analysis of

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

the over-time criteria relative to the single combined performance obligation may be similar to the analysis in Question F20. This analysis shows that the seller/developer will often recognize revenue over time because the seller/developer's performance creates or enhances an asset that the buyer controls as the asset is created or enhanced. [606-10-25-27(b)]

When there is just one performance obligation or unit of account for both the land sale and the construction services, however, the total revenue recognized over time represents the total transaction price (including the contract consideration for both elements). Progress toward satisfaction of that single performance obligation is measured relative to both elements (see Example F30.1).

When there is a single performance obligation or unit of account and the buyer does not hold title to the land or have legal ownership of the improvements affixed to the land as construction progresses (e.g. in some contracts to construct condominium units or similar structures), it may be difficult to conclude the performance obligation is satisfied over time. See additional discussion in Question F40.

Example F30.1
Sale of land with construction contract

Description of the arrangement

ABC Corp. sells land with a carrying amount of $400,000 to DEF Corp. for $1,000,000. Additionally, ABC agrees to build a fitness center for an additional $500,000 (estimated cost of $400,000).

ABC routinely provides construction services as an output of its normal activities but does not typically sell land.

Assume the sale of the land and the construction of the fitness center comprise two separate units of account (see additional discussion in Question C20) and DEF obtains the title to the land at closing before construction of the fitness center begins. ABC allocates $950,000 (of the total $1,500,000 transaction price) to the sale of the land and $550,000 to the construction contract, based on their relative stand-alone selling prices.

Evaluation

Because the sale of the land and construction of the fitness center comprise two separate units of account, ABC will need to determine when, or over what period, it satisfies each unit of account. ABC concludes that control of the land transfers when DEF takes legal and physical possession of the land. The construction services are satisfied over time because ABC is creating and enhancing an asset (the fitness center) that DEF controls as it is created.

For the land sale, ABC recognizes a $550,000 gain (allocated transaction price of $950,000 less the $400,000 carrying amount) at closing.

For the construction services, ABC uses an input method (cost-to-cost) to recognize revenue based on its periodic efforts relative to the total expected effort to completely satisfy the performance obligation.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Assume at the end of period one that the accumulated costs for constructing the fitness center are $200,000. Using costs incurred to measure its progress, ABC recognizes $275,000 of revenue ($550,000 × ($200,000 ÷ $400,000)) in period one. ABC recognizes the remaining revenue of $275,000 over time as it constructs the fitness center.

Question F40

Can the seller/developer of a condominium unit (or similar structure) recognize revenue over time as construction of the unit progresses if title to the completed unit does not transfer until construction is completed?

Interpretive response: To recognize revenue over time, the transaction must meet at least **one** of the following criteria. [606-10-25-27]

a. The customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs;

As discussed in Question F20, this criterion primarily applies to traditional service contracts (e.g. property management services) when the customer benefits on a periodic basis as the entity performs (e.g. as the property is being managed). This contrasts with service contracts when an asset is being constructed or enhanced on a customer's behalf that require further analysis under criterion (b) or under criterion (c) if criterion (b) is not met.

b. The entity's performance creates or enhances an asset (e.g. work in process) that the customer controls as the asset is created or enhanced; or

In many cases, we believe the buyer of a condominium unit is unable to direct the use of, and obtain substantially all of the remaining benefits from, the unit during construction because title to the real estate typically does not transfer until construction of the unit is complete and the sale closes. We also believe that the customer likely does not obtain substantially all the benefits of the unit because the buyer generally is unable to use the unit to:

- produce goods or provide services;
- enhance the value of other assets, settle liabilities or reduce expenses;
- sell or exchange the unit; or
- pledge the unit to secure a loan. [606-10-25-25]

The buyer also generally does not direct the use of the unit during construction because it does not hold legal title or have physical possession.

c. The entity's performance does not create an asset with an alternative use to the entity, and the entity has an enforceable right to payment for performance completed to date.

Topic 606 illustrates various scenarios when a seller/developer is constructing a unit in a multi-unit residential complex with differing customer payment structures.

Example 1 presumes the customer pays a deposit on entering into the contract, and the remainder of the contract price is payable on completion of

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

construction when the customer obtains physical possession of the unit. If the customer defaults on the contract before completion, the seller/developer only has a right to the deposit. The seller/developer does not have a right to payment for work completed to date so it does not meet criterion (c). [606-10-55-174 – 55-175]

Example 2 presumes the buyer makes progress payments during construction, and the contract has substantive terms that preclude the seller/developer from directing the unit to another customer. In addition, the contract precludes the buyer from terminating the contract unless the seller/developer does not perform, and if the buyer defaults on its payments, the seller/developer has the right to all of the consideration promised in the contract if it completes the unit. In this fact pattern, the seller/developer concludes that it meets criterion (c) because the:

- unit does not have an alternative use (i.e. the contract precludes the seller/developer from transferring the unit to another customer – see additional discussion below); and
- seller/developer has an enforceable right to payment for performance completed to date because the customer must pay all of the consideration promised in the contract if the seller/developer completes the unit.

The example points out that the legal practices in the particular jurisdiction are relevant in arriving at this conclusion. This is the case because if the contract terms provide for the right to payment for performance completed to date but the legal practices in the particular jurisdiction do not allow for enforcement of that right, criterion (c) would not be met. [606-10-55-176 – 55-180]

Example 3 presumes the same facts as Example 2 except in the event of the customer's default, the seller/developer can require the customer to perform as required under the contract, or it can cancel the contract and retain the unit under construction and assess a penalty in proportion to the contract price. The seller/developer has the right to payment for performance completed to date because it could enforce that right, even if the seller/developer also could choose to accept the unit under construction and assess a penalty instead. That choice does not affect the assessment as long as the seller/developer's right to require the customer to continue to perform under the contract is enforceable. [606-10-55-181 – 55-182]

While the examples primarily focus on the right to payment, even if a seller/developer does have the right to payment for performance completed to date (see Examples 2 and 3), it still needs to conclude the unit cannot be directed to another customer either contractually during construction or practically without incurring significant economic loss when it is completed. [606-10-25-28, 55-10]

We believe in many cases, buyers of condominium units cannot specify major structural changes to the design of the unit and the seller/developer often will be able to practically direct the unit to another buyer after completion. In those cases, a substantive contractual restriction **during** construction would need to be in place to conclude the seller/developer's performance does not create an asset with an alternative use to the seller/developer. If so, over time revenue recognition would be appropriate (and required) under criterion (c), assuming the seller/developer is entitled to payment for the work performed to date throughout the contract. The seller/developer should consider all facts and circumstances.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

If the seller/developer does not meet the criteria to recognize revenue over time, the performance obligation is satisfied at a point in time. The seller/developer would recognize revenue on the sale of a unit when control transfers to the customer, generally at closing as discussed in Question F10. In our experience, US condominium sales contracts generally are structured similar to the contract described in Example 1, which results in point-in-time revenue recognition when control of the completed unit transfers to the customer at closing. When a contract does not specify whether the entity has a right to payment on contract termination, we believe it is presumed that an enforceable right to payment does not exist. See Question F25 for additional discussion. [606-10-25-27]

If the seller/developer has a further obligation to develop an amenity in connection with the sale of the unit, the seller/developer would consider the guidance in Questions C10 and C20 on determining the number of performance obligations in the contract with the customer and Question F30 on the timing of revenue recognition.

See Question A60 for discussion about the unit of account for these sales under Topic 606.

Example F40.1
Sale of a condominium unit

Description of the arrangement

ABC Corp. is developing a condominium building and begins marketing individual units during construction. On January 1, 20X3, ABC enters into sales contracts with two customers to sell each one a unit with an estimated cost of $180,000 at a sales price of $300,000. Each customer provides a 5% down payment. Construction on the building is 50% complete.

ABC expects the customers to take possession of the units (and settle all remaining consideration) on January 1, 20X4; however, during construction ABC retains control of the building and the improvements. If the customers cancel the contracts, ABC has a right to only the deposit amount.

Evaluation

Because the arrangement does not meet any of the criteria for satisfying a performance obligation over time, ABC recognizes revenue at the point in time control transfers to the customers, generally when the customers take possession of the units on January 1, 20X4.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question F50

When does control transfer in a standstill arrangement in which a real estate subsidiary defaults on nonrecourse debt but the lender chooses to maintain the legal relationship until the lender can find a buyer?

Interpretive response: In these situations, the parent has to perform two derecognition analyses – one for the assets of the subsidiary and one for the liabilities.

Derecognition of the nonfinancial (and in-substance nonfinancial) assets

If substantially all of the fair value of the subsidiary is concentrated in nonfinancial assets, the parent applies Subtopic 610-20 to evaluate derecognition for each distinct asset within the subsidiary. See Question A20 [610-20-05-2]

Subtopic 610-20 requires the parent to evaluate derecognition of the real estate in two steps. As discussed in Question F90, in the first step, the parent evaluates whether it has lost its controlling financial interest under Topic 810. If the parent retains its controlling financial interest, it does not derecognize the real estate. We believe that in most standstill situations the parent will conclude that it no longer has a controlling financial interest in the entity. This is because the default provisions of most debt arrangements shift the power to direct the activities that most significantly affect the subsidiary's economic performance to the lender, even during the standstill period. [610-20-25-1 – 25-3]

If the parent loses its controlling financial interest, it moves on to the second step of evaluating derecognition under Subtopic 610-20. In the second step, under the principles of Topic 606, the former parent evaluates whether it has a contract with the lender and if so, whether it has transferred control of each distinct asset within its former subsidiary. [610-20-25-5 – 25-6]

As discussed in Question F90, Subtopic 610-20 has two models for evaluating whether the former parent has transferred control of the former subsidiary's assets. When the former parent retains a noncontrolling interest, the parent derecognizes each of the distinct assets when that former subsidiary controls those assets. When the former parent does not retain a noncontrolling interest in the former subsidiary, the parent derecognizes each of the distinct assets when the counterparty (or counterparties) controls those assets. [610-20-25-7]

While the application of these two models may yield different answers in a more traditional partial sale, we believe in this situation, the former parent will be evaluating whether it (as the legal owner of the former subsidiary) or the lender (as the counterparty to the transfer and the new parent of the subsidiary) controls the former subsidiary's assets after the default.

In making this determination, the former parent considers Topic 606's control indicators to determine if and when the lender obtains control. The following are indicators of the point in time that control has transferred:

— the transferor has a present right to payment for the asset;
— the counterparty has legal title to the asset;
— the transferor has transferred physical possession of the asset;

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

- the counterparty has the significant risks and rewards of ownership of the asset; and
- the counterparty has accepted the asset. [606-10-25-30, 610-20-25-6]

While the transfer of legal title and physical possession often are key indicators of control in the context of real estate sale transactions (see Question F10), we believe further analysis is necessary. In standstill arrangements, we believe the fact that the counterparty has the significant risks and rewards of ownership of the asset may be the most significant indicator of whether control has transferred.

For example, the guidance states that physical possession may not coincide with control of an asset in some repurchase or consignment arrangements when the customer has physical possession but the seller has control, and in some bill-and-hold transactions when the seller has physical possession but the customer controls. For a counterparty to have obtained control of a product (or asset) in a bill-and-hold arrangement, the transaction must meet all of the following criteria:

a. the reason for the bill-and-hold arrangement must be substantive – e.g. the counterparty has requested the arrangement;
b. the product must be identified separately as belonging to the counterparty;
c. the product currently must be ready for physical transfer to the counterparty; and
d. the transferor cannot have the ability to use the product or to direct it to another counterparty. [606-10-55-83, 25-30(c)]

We believe that in many standstill arrangements, the transfer will meet all of these criteria, which leads to the conclusion that the lender would have control even though the former parent maintains physical possession through its ownership interest in the subsidiary. In consideration of criterion (d), while the former parent continues to operate the property through the subsidiary during the standstill period (and therefore **uses** it), the lender may have the right to receive as debt service payments substantially all of the cash flows arising from the property's operations.

In addition, the former parent generally does not have the ability to sell the property (or its interest in the subsidiary) to another party, benefit from changes in the fair value of the property, or otherwise have the power to direct the activities that most significantly affect the property's economic performance (based on the guidance in Subtopic 810-10).

We believe the control analysis during the standstill period also is similar to the analysis performed when there is a repurchase option in place. This guidance indicates that the holder of an option to acquire the asset (the lender in this case) may presently control the asset even though the other party has physical possession. [606-10-55-66 – 55-71]

When the parent concludes it no longer has a controlling financial interest in the subsidiary and it no longer controls the assets within the former subsidiary, it derecognizes the assets and recognizes as a gain or loss equal to the difference between the amount of consideration it is entitled to receive and the carrying amount of the real estate. In this case, the consideration likely is limited to the carrying amount of the liabilities that the lender has promised to (or must) assume or relieve (after applying the constraint under Topic 606) when the standstill arrangement terminates. See Questions A20 and D50. [610-20-32-2, 32-5]

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Derecognition of the liabilities

Generally in standstill agreements, control of the real estate transfers before the liabilities are extinguished under Topic 405. In these situations, the seller recognizes the carrying amount of the liabilities (after applying the constraint as discussed above and in Question D50) as a contract asset. The contract asset represents the consideration that the former parent has not yet received in exchange for transferring the assets. [405-20-40-1, 606-10-32-11, 610-20-32-5, 45-3]

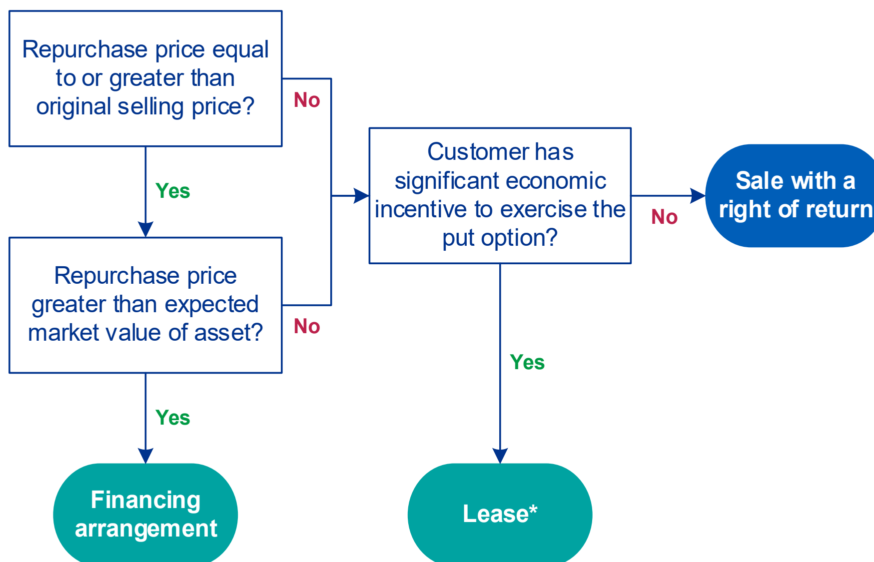
Question 17.4.20 of KPMG Handbook, Revenue recognition, provides additional discussion about recognizing contract assets and liabilities in a Subtopic 610-20 transaction.

Question F60

Has control transferred if in connection with the sale of real estate, the seller provides the buyer with an option to put the property back to the seller?

Interpretive response: Topic 606 provides guidance on accounting for a seller's obligation to repurchase a property at the buyer's request (a put option). The accounting for these transactions generally depends on the relationships between the repurchase price, the original selling price and the market value of the property. This guidance applies equally to transactions with noncustomers in the scope of Subtopic 610-20. [606-10-55-72 – 55-78, 610-20-25-6]

Put option
(a customer's right to require the seller to repurchase the asset)



* If the contract is part of a sale-leaseback transaction it is accounted for as a financing arrangement.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

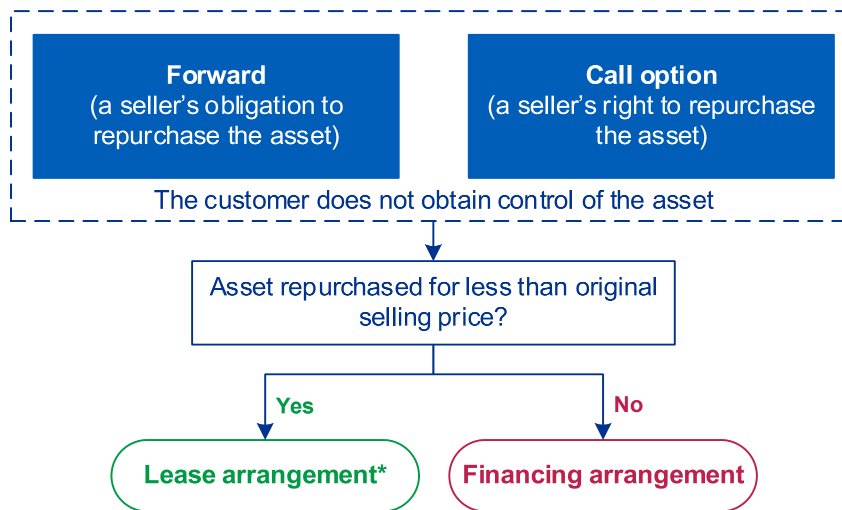
To determine whether the buyer has a significant economic incentive to exercise its put right, the seller considers the facts and circumstances including the relationship of the repurchase price to the expected market value of the property at the date of the repurchase (including consideration of the time value of money) and the amount of time until the right expires. If the repurchase price is expected to significantly exceed the market value of the property, this may indicate the buyer has a significant economic incentive to exercise the put option and require the seller to reacquire the property.

If the seller accounts for the contract as a financing arrangement, it continues to recognize the property and also recognizes a financial liability initially equal to the consideration received from the buyer. The seller recognizes amounts paid to the buyer above that amount as interest expense. If the option lapses unexercised, the seller derecognizes the property and the liability and recognizes revenue or gain. [606-10-55-70 – 55-71, 610-20-25-6]

Question F70

Has control transferred if in connection with the sale of real estate, the seller obtains the right (or has an obligation) to repurchase the property?

Interpretive response: Topic 606 provides guidance on accounting for a seller's right to repurchase a property (a call option) and a seller's obligation to repurchase a property (a forward). A seller's right under a call option (or obligation under a forward agreement) to repurchase the property precludes transfer of control to the buyer because the buyer is limited in its ability to direct the use of, and obtain substantially all of the remaining benefits from, the property even though it may have physical possession of the property. Whether the contract is accounted for as a lease or a financing depends on the relationship between the repurchase price and the original selling price. This guidance applies equally to transactions with noncustomers in the scope of Subtopic 610-20. [606-10-55-68 – 55-71, 610-20-25-6]



* If the contract is part of a sale-leaseback transaction, it is accounted for as a financing arrangement.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

While an option to repurchase the property at fair value arguably allows the buyer to obtain substantially all of the remaining benefits from the property, it limits the buyer's ability to direct the use of the asset. We believe sales subject to a seller's call option that is exercisable at fair value are accounted for as a leasing or financing arrangement depending on the expectation of the property's fair value over the option period relative to the original selling price. We expect these transactions generally to be accounted for as financing arrangements.

This guidance applies to both conditional and unconditional rights and does not permit or require an assessment of the probability that a conditional right will become unconditional. However, we believe if the condition that makes the right exercisable is controlled by the buyer, then a seller generally considers whether the buyer has the economic incentive to trigger the seller's right to repurchase (similar to the analysis on evaluating buyer put options). An example of when the buyer controls whether the seller can exercise the repurchase right is an anti-speculation clause in which the seller has the right to repurchase the property only if the buyer fails to comply with certain provisions of the sales contract. [606-10-55-72 – 55-78]

As discussed in Question F60, if the buyer has an economic incentive not to comply with the contract that triggers the seller's right to repurchase the asset, or there is greater than a remote likelihood the buyer will not comply for other reasons (notwithstanding its ability to comply with the contract), the contract is accounted for as a lease or a financing arrangement. That accounting depends on the relationship between the repurchase price and the original selling price.

If the buyer does not have a significant economic incentive to trigger the seller's right to repurchase the asset, and it is remote that the buyer would trigger the seller's repurchase right for other reasons, the seller follows the guidance on sales with a right of return that prevents recognition of revenue or gain only if the seller expects the buyer to return the property. [606-10-55-22 – 55-29]

In contrast, when the seller controls the right, we believe that generally the contingency should be ignored and the entity should account for the contract as a lease or financing arrangement because that right is no different than an unconditional right. However, if the option is not substantive, the entity should ignore the provision.

If neither the buyer nor the seller entirely controls the condition, the seller would consider the effect of the condition on the buyer's ability to control the asset. Remote contingencies such as a natural disaster generally do not preclude the buyer from obtaining control. However, a contingency that is more than remote may restrict the buyer's ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset for substantially all of its estimated useful life.

The following examples illustrate this point.

— When the buyer is obligated to stand ready to return the property for a period of time and cannot use up or consume the entire property until after the right lapses, the contract should be accounted for as a lease or a financing. This would also be true if the right restricted the buyer's ability to benefit from reselling the property because the property could only be sold

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

subject to the repurchase right. If the right expires, the seller would derecognize any liability and recognize revenue. [ASU 2014-09.BC424]

— When the condition is more than remote, but the right does not restrict the buyer's ability to direct the use or obtain substantially all the benefits of the asset, the conditional right may more appropriately be accounted for as a right of return.

Question F80

Is a right of first refusal (or a right of first offer) considered an obligation or right to repurchase the property?

Interpretive response: We do not believe a right of first refusal based on a bona fide offer by a third party constitutes an obligation or right to repurchase the property. Even if a seller of real estate includes a right of first refusal on the real estate as a condition of the sale, the buyer of that real estate still has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the property because:

- the buyer unilaterally controls the decision about whether and when to sell the asset; and
- if the buyer does decide to sell the asset, it will realize the asset's remaining benefits even if the original seller exercises its right because the original seller must match the amount offered by the third party.

We believe a similar conclusion applies to a right of first offer that allows the original seller to make an offer to the buyer before the buyer solicits or receives offers from third parties to resell the property. However, the buyer must be able to act in its best interest and must not be economically or contractually compelled to accept the offer, nor can the original seller be economically compelled to make an offer.

The guidance applies to both customer and noncustomer transactions.

Question F90

How should a seller evaluate transfer of control under Subtopic 610-20 when it transfers ownership interests in a legal entity (e.g. in a partial sale) or otherwise retains an interest in the asset (e.g. in a sale to an equity method investee)?

Interpretive response:

Transfer of control

As discussed in Question A20, Subtopic 610-20 applies when a parent derecognizes a subsidiary if substantially all of the fair value of that subsidiary is concentrated in nonfinancial assets. As discussed in Question F50, that

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

guidance requires the parent to evaluate derecognition of the underlying assets in two steps.

Step one

In the first step, the parent evaluates whether it has lost its controlling financial interest under Topic 810. If the parent retains its controlling financial interest, it does not derecognize the assets. Rather, it accounts for the sale of the noncontrolling interests under Topic 810's guidance covering decreases in ownership. That guidance requires the parent to recognize the transaction in equity. [610-20-25-1 – 25-3, 810-10-45-21A – 45-24]

Step two

If the parent loses its controlling financial interest, it moves on to the second step of evaluating derecognition under Subtopic 610-20. In the second step, using the principles of Topic 606, the former parent evaluates whether it has a contract with the buyer and, if so, whether it has transferred control of each distinct asset within its former subsidiary. [610-20-25-5 – 25-6]

Subtopic 610-20 has two models for evaluating whether the former parent has transferred control of the former subsidiary's assets. [610-20-25-7]

Former parent retains a noncontrolling interest

When the former parent retains a noncontrolling interest in the former subsidiary (i.e. the legal entity that holds the real estate), the parent derecognizes each of the distinct assets when that former subsidiary controls those assets. The former subsidiary controls those assets when it can direct the use of, and obtain substantially all of the benefits from, each distinct asset.

Because in most cases the subsidiary owns and controls the assets before the former parent sells the ownership interest in the subsidiary to a third party, we believe most partial ownership sales will result in gain recognition when the seller relinquishes its controlling financial interest in the subsidiary. Question 17.3.110 and Example 17.3.10 of KPMG Handbook, Revenue recognition, provide additional discussion about transfers of financial interests in legal entities.

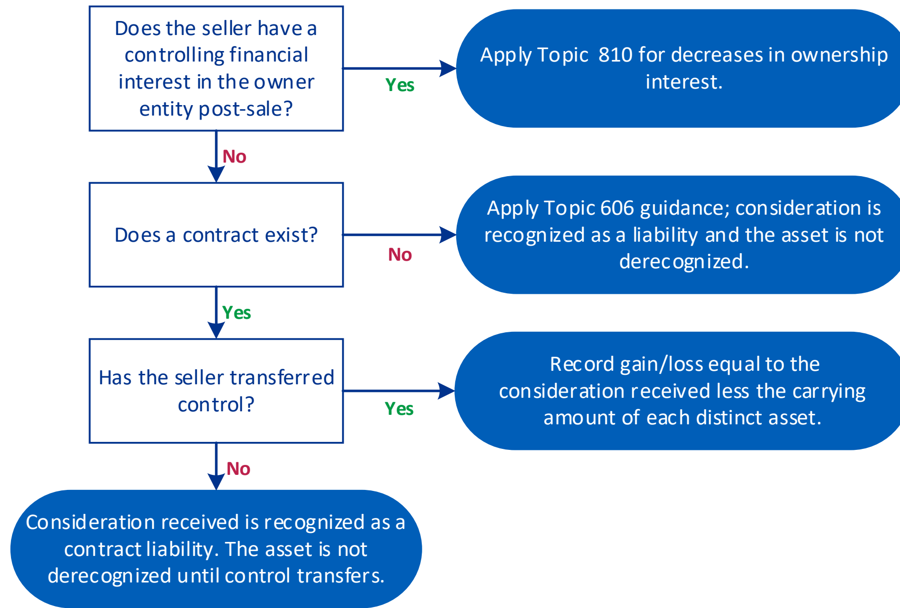
However, if the parent retains rights to individual assets held by the former subsidiary that constrain the subsidiary's ability to control the assets, control may not transfer until those rights expire. For example, if the parent retained a right (or had an obligation) to repurchase certain assets directly or purchase a controlling financial interest in the former subsidiary, the repurchase feature would prevent control of those assets from transferring to the former subsidiary. [610-20-55-15 – 55-16]

Former parent does not retain a noncontrolling interest

When the former parent does not retain a noncontrolling interest in the former subsidiary, the parent derecognizes each of the distinct assets when the buyer (or buyers) controls the assets. The buyer controls the assets when it can direct the use of, and obtain substantially all of the benefits from, each distinct asset.

The following flowchart depicts the decision sequence for evaluating control transfer.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.



Reminders on measurement

When the former parent transfers control of the assets, it derecognizes them and recognizes gains or losses equal to the differences between the allocated amount of consideration received and the carrying amount of each asset. The amount of consideration that is included in the calculation of the gain or loss includes both the **transaction price** and the carrying amount of liabilities assumed or relieved by the buyer (see Question D50).

As discussed in Question D40, the transaction price includes the fair value of noncash consideration the former parent receives in the form of a noncontrolling interest. By including the fair value of the noncontrolling interest in the transaction price, the former parent will recognize a 100% gain on these transactions when control of the nonfinancial (or in-substance nonfinancial) assets transfer to the counterparty.

Consider how the guidance is applied in the following transactions.

Transaction 1: A seller and a third-party investor form a venture. The seller contributes real estate to the newly formed venture and the third party investor contributes cash, property or services. The seller retains a controlling financial interest in the venture post-sale and no interest in the third party. Under Subtopic 610-20, because the seller retains a controlling financial interest in the venture, it applies the guidance in Topic 810 on decreases in ownership. The seller will not recognize a gain in income.

Transaction 2: Assume the same facts as Transaction 1 except the seller retains only a noncontrolling interest in the venture post-sale. The venture may be a joint venture. Under Subtopic 610-20, because the seller relinquishes its controlling financial interest in the venture and the former subsidiary controls the underlying assets, the seller measures its noncontrolling interest at fair value and recognizes a 100% gain in income from the derecognition of the underlying assets.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Transaction 3: A seller contributes real estate to a newly formed, wholly owned venture. Sometime later, it sells a partial ownership interest in the venture to a third-party investor for cash, property or services. The consideration may come directly from the investor to the seller or may be contributed by the investor to the venture. The seller retains a controlling financial interest in the venture post-sale and no interest in the third party. Under Subtopic 610-20, because the seller retains a controlling financial interest in the venture, it applies the guidance in Topic 810 on decreases in ownership. The seller will not recognize a gain in income.

Transaction 4: Assume the same facts as Transaction 3 except the seller has only a noncontrolling interest in the venture post-sale. The venture may be a joint venture. Under Subtopic 610-20, because the seller relinquishes its controlling financial interest in the venture and the former subsidiary controls the underlying assets, the seller measures its noncontrolling interest at fair value and recognizes a 100% gain in income from the derecognition of the underlying assets (see Example 17.3.50 of KPMG Handbook, Revenue recognition).

Transaction 5: A seller transfers real estate to an existing equity method investee for consideration. Under Subtopic 610-20, because the seller has only a noncontrolling interest in the investee and the investee controls the underlying assets, the seller measures a 100% gain in income from the derecognition of the real estate. If the transaction results in an increase in the seller's share of the investee's net assets, that amount is recognized at fair value.

Under the current guidance, the accounting is not affected by the form of the consideration received. The seller does not need to receive cash in the transfer to derecognize the assets and recognize a gain or loss. The seller can receive partially or entirely noncash consideration, including a noncontrolling interest in the investee, as long as it (a) no longer has a controlling financial interest in the entity holding the asset post-sale, and (b) has transferred control of the asset. [323-10-35-7(c), 610-20-15-4, 970-323-30-3]

Example F90.1

Partial sale with a retained controlling financial interest

Description of the arrangement

ABC Corp. and DEF Corp. form a venture, XYZ LLC. ABC contributes real estate with a carrying amount of $100 and receives $120 in cash from DEF and a 60% interest in XYZ. ABC has a controlling financial interest in XYZ post-transaction.

Evaluation

Because ABC has a controlling financial interest in XYZ post-transaction, the real estate is not derecognized and ABC accounts for the sale of the noncontrolling interest to DEF as an equity transaction under Topic 810.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

	Debit	Credit
Cash	120	
Noncontrolling interest ($100 carrying value × 40% noncontrolling interest in XYZ LLC)		40
Additional paid-in capital		80
To reflect cash received from DEF in exchange for 40% interest in XYZ.		

Example F90.2
Partial sale with a retained noncontrolling interest

Description of the arrangement

ABC Corp. and DEF Corp. form a venture, XYZ LLC. ABC contributes real estate with a carrying amount of $100 and a fair value of $300. ABC receives $180 in cash from DEF and a 40% interest in XYZ. ABC accounts for its investment in XYZ under the equity method post-transaction. XYZ controls the real estate post-transaction.

Evaluation

Because post-transaction (a) ABC has only a noncontrolling interest in XYZ and (b) XYZ controls the real estate, ABC derecognizes the real estate and recognizes a gain for the difference between the total consideration received and the carrying amount of the real estate. The total consideration received includes $180 in cash plus $120, equal to the fair value of the 40% noncontrolling interest in XYZ.

	Debit	Credit
Cash	180	
Investment in XYZ	120	
Real estate		100
Gain		200
To derecognize asset and recognize full gain on sale.		

Example F90.3
Sale to an existing equity method investee

Description of the arrangement

ABC Corp. owns 40% of XYZ LLC and accounts for its investment under the equity method. ABC sells to XYZ real estate with a carrying amount of $100 and a fair value of $300. The other investors in XYZ contribute $180 in cash to the venture to fund their portion of the purchase. ABC receives $180 in cash from

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

XYZ and maintains a 40% share in its underlying net assets. XYZ controls the real estate post-transaction.

Evaluation

Because post-transaction (a) ABC has only a noncontrolling interest in XYZ, and (b) XYZ controls the real estate, ABC derecognizes the real estate and recognizes a gain for the difference between the total consideration received and the carrying amount of the real estate. The total consideration received includes $180 in cash plus $120, equal to the increase in the value of ABC's share of XYZ's underlying net assets.

	Debit	*Credit*
Cash	180	
Investment in XYZ	120	
Real estate		100
Gain		200
To derecognize asset and recognize full gain on sale.		

ABC would recognize the same amount of gain if it had received $300 in cash rather than $180 in cash and $120 increase to its share of XYZ's underlying net assets.

Reminder on scope

The guidance discussed above applies only when the seller is transferring ownership interests in a subsidiary in which substantially all of the fair value is concentrated in nonfinancial assets.

When substantially all of the fair value of a subsidiary is not concentrated in nonfinancial assets, the seller would apply the guidance in Topic 810 on derecognition and decreases in ownership of businesses. This guidance is required for derecognition of subsidiaries when they are businesses and when no other guidance applies. Topic 810 requires full gain or loss in earnings when a controlling financial interest is sold, and no gain or loss in earnings when a controlling financial interest is retained (i.e. the gain or loss is recognized in equity). See Question A20.

Question F91

How is the transaction price allocated when the transaction contains multiple distinct nonfinancial assets?

Interpretive response: The entity allocates the transaction price (including amounts related to the liability assumed or relieved by the seller (see Question D50) to each distinct nonfinancial asset following Step 4 of the revenue recognition model. [610-20-25-5]

Generally, that results in an allocation to each distinct nonfinancial asset on a relative stand-alone selling price basis. Because of the nature of transactions

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

that are in the scope of Subtopic 610-20, it is not likely that an observable stand-alone selling price has been established for the nonfinancial asset. Therefore, the entity may have to estimate the stand-alone selling price.

Refer to Question C15 for additional guidance on the unit of account when the disposal group includes more than one asset and Question 17.3.130 of KPMG Handbook, Revenue recognition, for additional guidance on the unit of account in a partial sale.

Question F95

How is the gain or loss on the sale presented in the income statement?

Interpretive response: Subtopic 610-20 refers to the guidance in Topic 360 for presenting the gain or loss on the sale of long-lived assets. Under that guidance, the gain or loss that is not part of a discontinued operation is presented in income (loss) from continuing operations. If the entity presents a subtotal such as income (loss) from operations, the gain or loss is included in that subtotal. [610-20-45-1, 360-10-45-5]

Subtopic 610-20 does not provide guidance on presenting the gain or loss on sales of assets that are in its scope but are not long-lived assets. However, we believe entities generally should present the gain or loss consistent with the Topic 360 guidance applicable to long-lived assets.

In our experience, some entities include gains on disposals of long-lived assets in the same income statement line as impairment and disposal losses. Others include gains in an other income/expense or similar income statement line.

The SEC staff has stated that a registrant should report gains or losses that result from the disposition of long-lived assets as a component of other general expenses (i.e. in income from continuing operations) under Regulation S-X, with any material items stated separately. Further, the SEC staff has distinguished between other general expenses and selling, general, and administrative expenses, although both line items are included in operating income. [Reg S-X Rule 5-03(b)(6)]

An entity is required to disclose where the gain or loss is reported in the notes to the financial statements if it is not separately stated on the face of the income statement as described in paragraphs 360-10-50-3 and 50-3A. [610-20-50-1]

This guidance is reproduced from Question 17.4.10 in KPMG Handbook, Revenue recognition.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question F100

Does the guidance in Question F90 apply when the venture owns operating real estate that meets the definition of a business?

Interpretive response: No. As discussed in Question A20, Subtopic 610-20 applies only when the venture does not meet the definition of a business. If the asset (or subsidiary or group of assets) transferred meets the definition of a business, Subtopic 810-10 applies. However, in either case, the seller generally will recognize a 100% gain in income when it loses its controlling financial interest in the venture post-transaction, and $0 gain in income when it retains its controlling financial interest in the venture post-transaction. However, the amount of gain on the sale may differ depending on whether the asset (or subsidiary or group of assets) is a business or a nonfinancial asset because a seller would measure the consideration (a) at fair value in the derecognition of a business and (b) at the transaction price (which may include an estimate of variable consideration) plus the carrying amount of liabilities assumed by the buyer in the derecognition of a nonfinancial asset.

If contingent consideration is present in the contract, a difference in the gain or loss on derecognition between Subtopics 810-10 and 610-20 will likely occur because contingent consideration is accounted for at fair value under Subtopic 810-10, whereas it is accounted for as variable consideration subject to the constraint under Subtopic 610-20.

Question F110

Is a buy-sell clause allowing either investor to make an offer to acquire the other's interest in an entity that holds real estate considered an obligation or a right to repurchase the property from the perspective of the investor that sold the real estate to the entity?

Interpretive response: Frequently to facilitate a partial sale transaction, a seller will contribute property to a newly formed entity and a third party will contribute cash so that the seller can take a simultaneous cash distribution for the sale to that third party of an ownership interest in the entity. A contractual buy-sell clause may be included in the terms of the sale that enables both investors in the jointly owned entity to offer to buy the other investor's interest. In some cases, a buy-sell clause may be executed at any time; in other cases, only at a specified future date or if specified circumstances arise.

When an offer is made under the buy-sell clause, the recipient of the offer can elect to sell its interest for the offered amount or buy the offeror's interest at the offered amount. Generally, once an offer is made, the offeror is contractually required to buy the other investor's interest or sell its interest at the offered amount, depending on the other investor's election. A buy-sell clause can specify that the offer be at fair value, at a contractually specified amount, or at an amount determined by the offeror.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

We do not believe a buy-sell clause, by itself, precludes the buyer from obtaining control unless it gives the buyer an in-substance option to put its interest back to the seller or gives the seller an in-substance right to reacquire the buyer's interest in the property. If the buy-sell clause is an in-substance put or call option, the seller applies the guidance in Question F60 or Question F70.

A buy-sell clause may be considered an in-substance option when the buyer cannot act independently from the seller, or the seller is economically compelled to reacquire the other investor's interest in the jointly owned entity (reacquiring the property). Those circumstances suggest that the buyer's ability to direct the use of, and obtain substantially all of the remaining benefits from, the property is limited.

We believe the following indicators (not all-inclusive) may suggest the buyer has not obtained control.

a. The price specified in the buy-sell agreement indicates that the parties have already negotiated for the seller to acquire the buyer's interest. This would occur when the fixed price specified in the buy-sell clause economically compels the seller to acquire the buyer's interest or economically compels the buyer to sell its interest to the seller.

b. The seller has a strategic necessity or an investment strategy that indicates that it cannot relinquish its ownership rights to the buyer. Therefore, the seller is compelled to reacquire full ownership of the real estate.

c. The seller has arrangements with the jointly owned entity, such as management or third-party leasing arrangements, that may economically compel the seller to reacquire the real estate to retain the economic benefits (e.g. leasing commissions from lessees) or escape the negative economic consequences (e.g. a below-market contract with the entity).

d. Tax implications economically compel the seller to acquire the buyer's interest in the entity (thereby reacquiring the real estate).

e. Tax implications economically compel the buyer to sell its interest in the entity to the seller.

f. The buyer is financially unable to acquire the seller's interest.

g. The buy-sell clause stipulates a specified rate of return to the buyer (or seller), indicating that the buyer may not fully participate in the rewards of ownership from the real estate.

h. The buyer has a strategic necessity or an investment strategy that requires it to sell its interest to the seller.

i. The buyer is legally restricted from acquiring the seller's interest.

j. The real estate is integrated into the seller's business, so the buyer does not have alternative means available, such as selling to an independent third party, to realize its economic interest.

We believe this guidance applies to both customer and noncustomer transactions.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question F120

What is the accounting consequence when a general partner in a limited partnership sells a property to the partnership for cash (contributed by the limited partners) and a significant receivable?

Interpretive response: Under Topic 606 and Subtopic 610-20, the seller first determines if a contract exists given the significance of the receivable (see Question B10 for discussion about evaluating whether a contract exists and the resulting accounting if it does not). Next, it determines if and when control transfers (see Question F90).

Question F130

How should a manager recognize revenue associated with variable consideration in a property management services contract when the contract bases the variable consideration on a percentage of the property's operating results?

Interpretive response: As discussed in Question E10, the manager will need to determine if the services comprise a series of distinct time increments of property management services. Question C30 provides additional discussion about identifying the performance obligations in a property management services contract. If the manager concludes the services are a series of distinct services (i.e. a series of daily, weekly or monthly management services), it must allocate the variable consideration to the distinct service periods within the single, series performance obligation if:

a. the variable consideration earned for a given distinct service period relates specifically to the manager's services for that period (or an outcome from those services); and

b. allocation of that amount specifically to the distinct service period is consistent with the allocation objective. [606-10-32-40]

If the property management services comprise a series of distinct service periods to which the variable consideration earned each period can be allocated, the manager may not need to estimate the total variable fees that will be earned during the performance obligation period. The variable fees earned each period will be allocated to, and recognized in, each period.

Topic 606 provides an example of a 20-year hotel management service contract with a customer that pays the manager a monthly fee equal to 1% of the hotel's revenue. The manager concludes that it has a single performance obligation to provide a series of daily property management services and that its transaction price is entirely variable. [606-10-55-157B – 55-157E]

The property manager then must determine if and how to allocate the variable consideration to each of the distinct days of service in the series of daily services. The property manager concludes that the terms of the variable consideration relate specifically to the manager's efforts to transfer each

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

distinct daily service and, therefore, concludes that allocating the variable consideration based on the activities performed each day is consistent with Topic 606's overall allocation objective. See Question E10 for additional discussion about allocating the variable consideration. [606-10-32-39(b), 32-40]

When the contract only includes variable consideration based on a percentage of operating results, we believe in many cases a property manager will be able to apply the 'as-invoiced practical expedient' and recognize revenue in the amount to which it has a right to invoice. It will be able to apply the practical expedient because the terms of the contract intend to provide the property manager the right to consideration in an amount that corresponds directly with the value to the customer of the performance completed each period. [606-10-55-18]

Example F130.1

Multiple variable payments in one contract allocated to the period they were earned

Property Manager enters into a two-year contract to provide property management services to Customer. Property Manager charges Customer 2% of monthly occupancy fees, reimbursement of labor costs incurred to perform the service and an annual incentive payment based on 5% of gross operating profit.

Property Manager concludes that the contract consists of a single performance obligation satisfied over time to provide property management services. Property Manager also concludes that the performance obligation is a series of distinct days of service and that a time-based measure of progress is appropriate for the performance obligation.

Property Manager concludes that the contract has three types of variable consideration:

1. fee based on monthly occupancy fees;
2. reimbursement of variable labor costs; and
3. annual incentive payment based on gross operating profit.

Property Manager evaluates whether those amounts should be allocated entirely to one or more distinct service periods.

1. Monthly fee. Property Manager concludes that the entire fee should be allocated each month. The variable amounts relate directly to Property Manager's efforts and the outcome from providing the services each month and are not dependent on prior or future months' services and meet criterion (a) in Question F130. Further, criterion (b) in Question F130 is met because the percentage of rental revenue is consistent each month and would depict the amount the entity would charge to provide those services on a monthly basis.

2. Reimbursement of variable labor costs. Property Manager concludes that the fee should be allocated entirely to each day. The variable amounts relate directly to Property Manager's efforts to transfer the service in that time period and meet criterion (a) in Question F130 because it is resolved each day (i.e. not dependent on past or future performance). Further, criterion (b) in

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question F130 is met because the reimbursement pricing structure remains consistent among the distinct daily service periods and depicts the varying amounts of consideration to which the entity expects to be entitled each day.

3. Annual incentive payment. Property Manager concludes the annual incentive payment relates directly to the benefit provided to the customer for the annual period and it is consistent with incentive fees that could be earned in other years. As such, Property Manager concludes the incentive payment should be allocated to each year.

Property Manager not only considers the allocation of the payments individually, but also considers the allocation of all of the payment terms. As such, because the monthly reimbursement of variable labor costs and annual incentive payment relate to different service periods, Property Manager needs to consider whether allocating the fees to different periods is consistent with the allocation objective. Property Manager concludes that allocating the monthly occupancy fee, reimbursement of variable labor costs and annual incentive payment to different periods is consistent with the allocation objective because each day during the contract period is in effect allocated its proportion of the variable consideration.

Question F140

When should a real estate broker that is acting as an agent recognize revenue?

Interpretive response: A real estate broker often provides an agency service to its customer when it is not the principal in the transaction but instead performs a service of arranging for the provision of a good or service (e.g., the transfer of control of the real estate) between the parties to a real estate transaction. A real estate broker could either be the agent for a party selling or leasing property or represent the buyer/lessee in the transaction.

The timing of revenue recognition first depends on whether the entity satisfies the performance obligation at a point in time or over time. If the performance obligation is satisfied over time, the real estate broker would apply an appropriate measure of progress. If not satisfied over time the broker would need to determine the point in time it satisfies that performance obligation.

When a similar activity is bundled with other property management services, the entity will first need to consider whether the service is distinct from the other activities. See Question C30 for additional discussion.

Over time vs point in time

A real estate broker acting as a sales agent for a customer that receives a commission when the deal closes generally satisfies its performance obligation at a point in time. This is because the activities performed by the broker before sale typically do not transfer a good or service to a customer. If the customer receives any benefit from the entity's activities before the sale, that benefit generally is limited unless the sale is completed. These services typically do not meet the over-time criteria because:

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

— the customer does not simultaneously receive and consume benefits as the broker performs;
— the broker is not creating or enhancing an asset the customer controls; and
— the broker does not have an enforceable right to payment for performance to date. [606-10-25-27]

However, there may be arrangements that provide benefits to the customer over time before a sale is completed. For example, this may arise when a broker that enters into a written sale agent agreement receives a significant nonrefundable upfront fee at the time of listing and a relatively small commission fee when a sale is completed. The large nonrefundable upfront fee generally indicates that the broker is providing the customer with a listing or marketing service and the customer is benefiting from that service over time. Moreover, that transaction likely meets the over-time criteria if the upfront fee compensates the entity at cost plus a reasonable margin for its performance to date and its performance does not create an asset with alternative use to the entity (see Question F40 for further discussion of the over-time criteria).

Satisfaction of a point-in-time performance obligation

When a broker satisfies its point-in-time agency performance obligation can vary based on the facts and circumstances. For example, a broker may satisfy its performance obligation when the principal and the end customer have each committed to the contract or when the specified good is delivered or specified service provided. In an agency relationship, the timing of when the principal transfers control of the specified good or service to the end customer may differ from the timing of when the agent satisfies its performance obligation.

There are multiple factors that can affect the point in time that an agent's performance obligation to arrange for the provision of a specified good or service is satisfied. The following are important factors that we believe influence this determination.

Who is the agent's customer? Agency relationships typically involve the agent entering into contractual agreements with different counterparties. An agent's customer for its agency service may be the principal in the contract, the customer purchasing the specified good or service, or both.

Determining its customer(s) is key to the agent establishing the nature of its agency service – i.e. the nature of its promise to that (those) customer(s) and when the related performance obligation is satisfied. For example, the nature of an agent's promise may be different depending on which party in the real estate transaction the agent is representing.

What is the nature of the agent's promise to its customer(s)? Topic 606 establishes that an agent 'arranges for provision of the specified good or service' by the principal. However, it does not provide further guidance about what that promise entails. The agent's promise to its customer may involve more than 'connecting' the two parties. For example, the agent may:

— provide a value-add service, such as consulting, after the specified good is delivered or specified service is provided; and/or

— continue to perform a customer service function after the parties have entered into their contract(s) – e.g. interfacing with the end customer about coordinating closing documents and procedures or the move-in between the end customer and the principal.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

The first example likely represents a performance obligation (for which the entity is a principal) separate from the agency service, and therefore would not affect the timing of satisfaction of the agency service. However, judgment may be involved in deciding whether a customer service function is a separate performance obligation – i.e. separate from the agency service – or an integral **part of** the agent's promise to provide the agency service and whether the entity has completed its agency service.

If the entity is an agent for a specified good or service and also a principal for another performance obligation in the contract, the entity will need to allocate the consideration between the two performance obligations.

Determining the nature of the entity's promise to provide the agency service is critical to determining when that performance obligation is satisfied. How this affects the timing of agency revenue recognition is illustrated in Example F140.1.

In some cases, the point at which the broker has a right to payment may be informative, although not determinative, when evaluating the nature of the broker's promise. For example, when a broker has a right to payment without further performance it may indicate that the nature of the promise corresponds to the activity that triggers the payment. However, a broker will need to distinguish between payment terms that represent variable commission and payment terms that correspond to the entity's performance. See trailing commissions below for further discussion.

When does the principal transfer control of the specified goods or service to the end customer? The principal's transfer of control of the specified good or service to the end customer may indicate the agent's performance obligation is satisfied.

For example, an agent may continue to perform an important customer service function, interfacing with the principal on the end customer's behalf about matters such as timing of close or coordination of the move-in, before control of the specified good or service transfers to the end customer. However, after control transfers (or begins to transfer in the case of a specified service satisfied over time), that availability may no longer be an integral part of its promise to arrange for the provision of the specified good or service – even if the agent remains available to the end customer as a matter of customer relationship – because the end customer may have access to information or to the service provider that it did not have previously. For example, the customer may now have direct access to the landlord.

Trailing commissions

Trailing commissions often occur when a real estate broker satisfies its agency performance obligation and receives subsequent payments from the principal entity based on factors outside of the broker's control – e.g. each time the tenant renews a lease or in some cases when the lease term commences. When the broker has no further obligations to the principal entity or the end customer after the point in time the initial agency performance obligation is satisfied, it determines the amount of trailing commissions to recognize as revenue when the initial performance obligation is satisfied by applying the guidance on variable consideration. If the entity performs other tasks that occur after the initial sale, judgment will be required to determine whether those activities represent performance obligations and therefore may affect the

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

allocation of the trailing commissions and the timing of revenue recognition. [606-10-32-11]

A real estate broker estimates trailing commissions at contract inception and includes them in the transaction price, subject to the variable consideration constraint (see Question D10). A real estate broker with a significant amount of history selling a particular product or service will likely recognize a portion of revenue related to anticipated trailing commissions at the point in time the performance obligation is satisfied. When there is a lack of history or the trailing commissions are based on other significant uncertainties (e.g. market volatility), the application of the variable consideration constraint guidance may be challenging. However, in many circumstances we would expect a real estate broker to be able to estimate at least some portion of the trailing commissions at the time the performance obligation is satisfied.

A real estate broker reassesses its estimate of anticipated trailing commissions at each reporting date, and records revenue for those anticipated trailing commissions when it becomes probable that a significant reversal in cumulative revenue recognized related to those trailing commissions (or a portion thereof) will not occur.

Example F140.1
Real estate broker commissions

ABC real estate broker provides various brokerage services to assist customers in leasing or selling real estate. ABC receives a commission for services based on different commission structures.

Scenario 1: 100% commission upon lease execution

ABC enters into a contract to represent Landlord to lease space. ABC earns 100% of its commission on execution of the lease. The commission is due and nonrefundable regardless of whether the tenant ultimately takes possession of the space. ABC does not have any substantive performance requirements and does not perform any substantive services for Landlord or a prospective tenant after lease execution. After lease execution, Landlord handles the relationship with the tenant.

ABC determines that the contract includes a single agency performance obligation related to brokering a lease between Landlord and a prospective tenant.

Over time vs point in time

ABC evaluates whether the agency performance obligation is satisfied over time or at a point in time and evaluates the over-time criteria as follows:

- Landlord does not consume and receive benefit from the services as ABC performs because those activities do not transfer a good or service to Landlord and the benefit of the activities generally is limited unless the lease is executed. Further, another entity would have to substantially re-perform the activities to find a prospective tenant.
- ABC does not create or enhance an asset that the building owner controls while the asset is created or enhanced.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

- ABC does not have an enforceable right to payment for performance completed to date. ABC will only earn the commission upon successfully brokering an executed lease between the building owner and prospective tenant.

Because none of the criteria for over-time revenue recognition are met, ABC concludes the revenue from the leasing commission should be recognized at a point in time.

Satisfaction of point-in-time agency performance obligation

ABC evaluates when it satisfies the point-in-time agency performance obligation and considers the factors in Question F140.

- **Who is ABC's customer**? Landlord is ABC's customer as it is the party that ABC entered into the contract with and agreed to represent.
- **What is the nature of the ABC's promise to its customer?** The nature of ABC's promise to Landlord is to execute a lease agreement. This is evidenced by the fact that ABC has a right to consideration upon lease execution and does not perform any substantive services for Landlord or tenant after the lease is executed.
- **When does the principal transfer control of the specified goods or service to the end customer?** The specified lease service transfers to the tenant when the lease term commences.

Based on the above, ABC concludes that the nature of its promise to Landlord (its customer) is to provide an executed lease and that is the point in time at which ABC's services are complete. As a result, ABC recognizes revenue at lease execution.

While the specified lease service does not transfer from Landlord to tenant (the end customer) until lease commencement, ABC is not required to perform and does not perform any substantive services between lease execution and lease commencement and therefore the performance obligation is satisfied at lease execution.

Scenario 2: 50/50 lease commission structure

Assume the same facts as Scenario 1 except that ABC is entitled to only 50% of the commission upon lease execution and is entitled to the remaining 50% when the lease commences (i.e. when the tenant moves in). The initial 50% payment is nonrefundable regardless of whether the tenant moves in.

While ABC only receives 50% of the commission upon lease execution, ABC does not have substantive performance requirements after lease execution and the second 50% payment is variable consideration. As a result, even though the payment structure is different than Scenario 1, ABC still recognizes revenue at the point in time the lease is executed.

ABC estimates the variable consideration (i.e. the second 50% payment) using a most likely outcome approach (subject to the constraint) and recognizes that amount of revenue at the time of lease execution.

Scenario 3: Real estate sale

ABC enters into a contract to represent Seller in the sale of real estate to a prospective buyer. Seller will receive a fixed purchase price and contingent consideration equal to 5% of future operating profits of the property over a

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

3-year earn-out period. ABC earns a sale commission equal to a percentage of the fixed purchase price when the transaction closes. ABC will also earn a percentage of the future contingent consideration paid by the prospective buyer to Seller over the 3-year earn-out period. If the sale falls through, ABC is not entitled to a payment.

ABC is required to perform activities necessary to obtain execution of a binding purchase and sale agreement between Seller and prospective buyer, activities performed during the due diligence period, and continuously represent the buyer through actual legal close of the sale transaction. ABC is not required to perform any activities during the 3-year earn-out period.

ABC determines that the contract includes a single performance obligation to broker the sale transaction and that all of the activities prior to close are activities that ABC performs to fulfill its promise to Seller.

Over time vs point in time

ABC considers whether the agency performance obligation is satisfied at a point in time or over time as follows:

- Seller does not consume and receive benefit as ABC performs the pre-sale activities because those activities do not transfer a good or service to Seller and the benefit of the activities generally is limited unless the transaction closes. Further, another entity would have to substantially re-perform the activities to find a prospective buyer. This would be the case even after ABC identifies a prospective buyer because the new agent would need to re-perform the work in the event the transaction with that prospective buyer fell through.
- ABC does not create or enhance an asset that the current owner controls as the asset is created or enhanced; and
- ABC does not have an enforceable right to payment for performance completed to date. The sale commission is only payable to ABC upon the close of the sale.

As none of the criteria for over-time revenue recognition are met, ABC concludes the revenue from the sale commission should be recognized at a point in time.

Satisfaction of point-in-time agency performance obligation

Next, ABC evaluates when it satisfies the point-in-time agency performance obligation and considers the factors in Question F140.

- **Who is ABC's customer**? Seller is ABC's customer because it is the party that ABC entered into the contract with and agreed to represent.
- **What is the nature of the ABC's promise to its customer?** The nature of ABC's promise to Seller is to arrange for a closed sale transaction. This is evidenced by ABC's requirement to perform until close and the fact that ABC is not entitled to consideration until close.
- **When does the principal transfer control of the specified goods or service to the end customer?** Control of the underlying real estate transfers to the buyer at close.

ABC concludes that the nature of its promise to Seller (its customer) is to arrange for a closed sale transaction, and closing is the point in time at which

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

ABC's obligation is satisfied. While ABC only receives a commission equal to a percentage of the fixed purchase price at sale closing, ABC does not have substantive performance requirements after the sale closes. As a result, ABC concludes that revenue is recognized at the point in time the sale closes.

ABC estimates the variable consideration (i.e. payments related to contingent consideration during the 3-year earn-out period) using an expected value approach and evaluates whether the amount is constrained. ABC recognizes the amount included in the transaction as revenue at the time of sale closing.

At each future reporting period during the 3-year earn-out period, ABC reassesses its estimates of future commission payments and recognizes additional revenue from anticipated commissions to the extent that does not make it probable that a significant reversal of cumulative revenue recognized will occur.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

G. Other implementation matters

Questions and Examples

Q&A G10 For transition purposes, how would an entity apply the definition of a completed contract when a reduced profit method under legacy US GAAP was being used?

Example G10.1: Not a completed contract at transition

Example G10.2: Not a completed contract at transition

Q&A G15 For transition to Subtopic 610-20, is a partial sale a completed contract?

Example G15.1: Partial sale at transition

Q&A G20 How does Topic 606 interact with Topic 842 (when adopted) when the lease is an operating lease and the lessee pays for certain services and lessor costs – e.g. common area maintenance and property taxes?

Q&A G22 If a lessor separates lease and non-lease components, how should it estimate the stand-alone selling price of CAM to allocate total consideration for an operating lease?

Q&A G23 If a lessor separates lease and non-lease components, should it allocate variable CAM charges entirely to the CAM non-lease component? Should a lessor allocate any of the fixed lease payment to the CAM non-lease component?

Q&A G24 If a lessor separates lease a CAM non-lease component, how should it determine the number of performance obligations?

Q&A G25 If a lessor separates a CAM non-lease component, how should it allocate variable CAM payments (and recognize revenue) when CAM is determined to be a series of distinct service periods?

Q&A G26 How should a lessor account for CAM provided in a lease after it adopts Topic 606 but before it adopts Topic 842?

Q&A G27 After adopting Topic 842, how should a lessor present in its income statement CAM revenue and lease income?

Q&A G28 Is a lessor permitted to recast comparative periods to conform to its Topic 842 presentation of revenue from lease and qualifying non-lease components?

Q&A G29 Is a lessor permitted to recast comparative periods to conform to its Topic 842 gross vs net presentation?

Q&A G30 Does Subtopic 340-40 change whether an entity can capitalize costs incurred to sell real estate projects?

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question G10

For transition purposes, how would an entity apply the definition of a completed contract when a reduced profit method under legacy US GAAP was being used?

Interpretive response: When an entity adopts Topic 606 and Subtopic 610-20, it uses one of the following two transition methods.

Method 1

Retrospectively by restating each prior period before the date of initial application that is presented in the financial statements (full retrospective). An entity also may elect retrospective application with or without a number of practical expedients.

Method 2

Recording the cumulative effect of initially applying Topic 606 and Subtopic 610-20 as an adjustment to the opening balance of equity at the date of initial application (no restatement of comparative prior periods). An entity may apply the cumulative effect transition approach either to (a) only those contracts that are not **completed contracts** at the date of initial application or (b) all contracts.

Topic 606 defines a completed contract for transition purposes as one for which all (or substantially all) of the revenue was recognized under legacy US GAAP. Real estate sales that have occurred before the date of initial application and met the criteria for full accrual profit recognition under Subtopic 360-20 generally would be considered completed contracts and therefore no adjustment to opening equity would be needed for those transactions (because the adjustment would only be necessary for contracts that are not completed). However, if the seller applied a reduced-profit method for a real estate sale under legacy US GAAP (e.g. the installment method), the contract will not be completed unless substantially all of the revenue has been recognized at the adoption date. [606-10-65-1(c)(2)]

For noncustomer transactions, we believe a seller should identify completed contracts by determining whether the gain recognized has been measured using all or substantially all of the **sales value**.

Sales value is:

— the stated sales price; plus
— other amounts that are in-substance sales proceeds (like option proceeds); minus
— discounts to reduce receivables to net present value; minus
— the net present value of future services the seller has agreed to provide without compensation or at less than prevailing rates. [360-20-40-8]

We believe the **stated sales price** includes stated consideration that is not fixed or realized at closing. For example, if the sale includes cash at closing and a future profits interest, we believe an estimate of the future profits interest is part of the total sales value when determining whether all or substantially all of the revenue was recognized under legacy GAAP. Accordingly, we believe a real estate sale qualifying for full accrual profit recognition under Subtopic 360-20 would not be considered a completed contract in circumstances where there is

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

an ongoing earn-out or other interest in future profits that prevents the entity from being able to conclude that substantially all of the sales value has been recognized before the date of initial application.

Example G10.1

Not a completed contract at transition

Description of the arrangement

ABC Corp. sells a property to DEF Corp. (a customer) for $10,000,000 with a carrying amount of $8,000,000. ABC receives $500,000 at closing on October 1, 2019 and finances the remaining $9,500,000 under a 30-year note receivable. Because DEF's initial investment of $500,000 is not adequate, ABC accounts for the transaction under the installment method prescribed by Subtopic 360-20 (assuming the criteria for the installment method are met). DEF makes its first principal payment on the note of $100,000 on December 31, 2019.

ABC has a calendar year-end and for purposes of its 2019 annual financial statements, ABC recognizes $600,000 of revenue, $120,000[16] profit on the sale of the property, and deferred profit of $1,880,000.

Evaluation

ABC adopts Topic 606 on January 1, 2020 and concludes its contract is not complete because it has not recognized substantially all of the $10,000,000 revenue under legacy US GAAP (Subtopic 360-20).

Under the retrospective method, ABC would recast its 2019 financial statements to reflect the property sale under the guidance of Topic 606. If ABC concludes that a contract existed in 2019 (including that the collection of the note is probable) and control of the property transferred, then its 2019 financial statements would be recast to reflect revenue of $10,000,000 and profit on the sale of the property for the full $2,000,000 (or gain on sale of $2,000,000 for a transaction with a noncustomer).

Under the cumulative effect method, ABC does not recast its 2019 financial statements (i.e. revenue of $600,000 and profit of $120,000 recognized in 2019 is unchanged). However, if ABC concludes that a contract existed in 2019 (including that the collection of the note was probable) and control of the property transferred, then it records a cumulative effect adjustment of $1,880,000 to increase opening equity (retained earnings) and derecognizes the property on January 1, 2020.

Conversely, if it concludes that a contract did not exist, then it would record a cumulative effect adjustment of $120,000 to decrease opening equity (retained earnings) on January 1, 2020 and would continue to recognize the property at its depreciated carrying amount.

[16] $2,000,000 profit ÷ $10,000,000 sales price × $500,000 received at closing plus $2,000,000 profit ÷ $10,000,000 sales price × $100,000 principal payment.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Example G10.2
Not a completed contract at transition

Description of the arrangement

ABC Corp. sells a newly constructed retail property with a cost of $1,200,000 to DEF Corp. (a customer) for $2,000,000 and a right to receive 25% of future operating profits from the property over a 10-year earn-out period. ABC receives cash of $2,000,000 on October 1, 2019 at closing and expects to collect an additional $420,000 over the earn-out period. ABC has no other continuing involvement in the property and meets all the criteria for full accrual profit recognition under Subtopic 360-20.

In its 2018 financial statements, ABC recognizes revenue of $2,000,000 and profit of $800,000 on the sale of the property and $10,000 of contingent profit for the amounts realized in the period October 1 through December 31, 2019. ABC would recognize a gain of $800,000 on the sale if the transaction were with a noncustomer.

Evaluation

ABC adopts Topic 606 on January 1, 2020 and concludes its contract for the property sale on October 1, 2019 is not complete because it has not recognized substantially all of the expected revenue of $2,420,000 ($2,000,000 + $420,000) under legacy US GAAP (Subtopic 360-20).

Under the retrospective method, ABC would recast its 2018 financial statements to reflect the property sale under the guidance of Topic 606. If ABC concludes that a contract existed in 2019 and control of the property transferred, then it would recast its 2019 financial statements to reflect revenue of $2,420,000 and profit on the sale of the property for the full $1,220,000, assuming the variable consideration of $420,000 (representing the future profits interest) is not constrained. ABC would recognize a gain of $1,220,000 if the transaction were with a noncustomer.

Under the cumulative effect method, ABC does not recast its 2019 financial statements (i.e. profit recognized in 2019 of $810,000 is unchanged). However, if ABC concludes that a contract existed in 2019 and control of the property transferred, then it records a cumulative effect adjustment of $410,000 (total profit under Topic 606 of $1,220,000 minus $810,000 recognized before adoption) to increase opening equity (retained earnings) on January 1, 2020 and derecognizes the property.

Question G15
For transition to Subtopic 610-20, is a partial sale a completed contract?

Interpretive response: Under legacy US GAAP, when a seller executed a partial sale and kept only a noncontrolling interest, it recognized a partial gain – i.e. the gain attributable only to the portion sold to the third party. The noncontrolling interest held by the seller was characterized as a retained interest in the asset sold and was measured at carryover basis. As discussed in

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question F90, under Subtopic 610-20, when a seller executes a partial sale and keeps only a noncontrolling interest, it recognizes 100% gain. The noncontrolling interest held by the seller is characterized as contract consideration and is measured at fair value.

As discussed in Question G10, Topic 606 defines a completed contract for transition purposes as one for which all (or substantially all) of the revenue was recognized under legacy US GAAP. [606-10-65-1(c)(2)]

For noncustomer transactions, we believe a seller should identify completed contracts by determining whether the gain recognized has been measured using all or substantially all of the sales value. In applying that guidance to a partial sale, we believe a seller should evaluate whether the gain recognized was measured using all or substantially all of the sales value received from the third party in exchange for the partial ownership interest. The sales value would not include the fair value or the carrying amount of the ownership interest retained because Subtopic 360-20 did not characterize the retained interest amount as part of the consideration received and the analysis of whether a contract is complete is based on legacy GAAP.

Example G15.1
Partial sale at transition

Description of the arrangement

ABC Corp. and DEF Corp. formed a venture in 2015, XYZ LLC. ABC contributed real estate with a carrying amount of $100 and a fair value of $300. ABC received $180 in cash from DEF and a 40% interest in XYZ. There was no other consideration in the contract.

ABC recognized a gain of $120 (($300 - $100) × 60%) for the 60% interest sold and an equity method investment with an initial carrying amount of $40.

Had ABC accounted for this transaction under Subtopic 610-20, it would have recognized a gain of $200 and an equity method investment with an initial carrying amount (equal to its fair value) of $120. See Example F90.2.

Evaluation

ABC's contract with DEF is *completed* because the gain recognized has been measured using all of the sales value from DEF under Subtopic 360-20 ($180).

Question G20
How does Topic 606 interact with Topic 842 (when adopted) when the lease is an operating lease and the lessee pays for certain services and lessor costs – e.g. common area maintenance and property taxes?

Interpretive response: For more information on Topic 842's effective date, see Question A30 and KPMG Handbook, Leases.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Accounting for non-lease components – e.g. CAM

A contract might contain non-lease components in addition to lease components. For example, in addition to leasing office space, the lessor may promise to provide common area maintenance services (CAM), such as cleaning of common areas, snow removal, parking lot maintenance and repairs. In these situations, CAM is a non-lease component of the contract – i.e. service being provided to the lessee. [842-10-55-144 – 55-145]

The accounting for non-lease components depends on whether the lessor elects the practical expedient allowing it not to separate components that would be within the scope of Topic 606 if accounted for separately.

Topic 842 allows the lessor to elect not to separate non-lease components that would be accounted for under Topic 606 – e.g. CAM, if two criteria are met: [842-10-15-42A]

a. the timing and pattern of transfer to the lessee of the lease component and the non-lease component(s) associated with that lease component are the same; and

b. the lease component, if accounted for separately, would be classified as an operating lease.

Lessor elects the practical expedient

If the lessor has elected the practical expedient and a contract includes multiple non-lease components—one or more that meet the timing and pattern of transfer criterion and one or more that do not—the lessor combines the non-lease components that meet the criterion with the lease component and separates any non-lease components that do not. [842-10-15-42C]

If the non-lease components are the predominant components of the combined component, the lessor should account for the combined component under Topic 606, as a single Topic 606 performance obligation, rather than the leases guidance in Topic 842. In those cases, the lessor: [842-10-15-42B]

— uses the same measure of progress for the combined Topic 606 component as it used when determining eligibility for the combination of lease and non-lease component(s) (generally, time-elapsed); and

— accounts for all variable payments related to any good or service, including the lease, that is part of the combined Topic 606 performance obligation using the guidance on variable consideration in Topic 606.

Otherwise, the combined component is accounted for under Topic 842 as an operating lease. This includes circumstances when the lease component and non-lease component(s) are equally significant to the contract. [842-10-15-42B]

In many cases, determining whether to account for the combined component as a lease or as a single non-lease component in the scope of Topic 606 will be simple. For example, in most real estate lease scenarios that include CAM, it will be clear that the lease is the predominant element of the combined component. This is because the lessee would clearly be expected to ascribe more value to its right to use the real estate than to the CAM services.

A lessor elects the practical expedient by class of underlying asset. [842-10-15-42A]

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Lessor does not elect the practical expedient or the lease and non-lease component(s) do not qualify for combination

If the lessor does not elect the practical expedient or the lease and non-lease component(s) do not meet the required criteria for combination, the lessor should separate the lease and the non-lease components (e.g. the office space lease and relevant non-lease component) and allocate the consideration in the contract using the requirements in Topic 606 for allocating the transaction price (i.e. generally on a relative stand-alone selling price basis). [842-10-15-31, 606-10-32-28 - 32-41, 842-10-15-28 – 32, 15-38 – 15-42]

The allocated revenue associated with the non-lease component(s) will be recognized under Topic 606 and the allocated lease income associated with the lease component(s) will be recognized under Topic 842. See Question G22 for additional discussion. [606-10-32-28 – 32-29, 842-10-15-38 – 15-42]

Accounting for elements that are not 'components' – e.g. property taxes or insurance paid to or on behalf of the lessor

Not every element of a contract that contains a lease is necessarily a 'component' (lease or non-lease). While it may be intuitive to assume that any activity or cost that is not a lease component or payment that is not an explicit 'lease payment' must be a non-lease component, this is not how Topic 842 works. Instead, some elements of a contract – i.e. some activities and/or payments – are not components because they do not transfer a good or service to the lessee. [842-10-15-30]

Examples of elements of a lease contract that do not transfer a good or service to the lessee include a lessee's reimbursement or payment of the lessor's property taxes and insurance. The lessee does not receive a good or service from having to reimburse the lessor, or directly pay, the lessor's property taxes to the relevant taxing authority. Similarly, the lessee does not receive a good or service from reimbursing the lessor's insurance premium on the real estate asset or paying for insurance in its own name on an asset that primarily benefits the lessor (see section 4.2 of KPMG Handbook, Leases). [842-10-15-30]

The accounting for property taxes and insurance paid for by the lessee will be based on who (the lessee or the lessor) pays the relevant third party (e.g. the taxing authority or the insurance provider) for the cost.

- If the lessee pays the third party directly – e.g. remits payment of the tax directly to the taxing authority or pays the insurance premium to the insurer – the lessor will recognize the cost and the lessee's payment net in the income statement. Neither the lessor's costs nor the lessee's payments will be reflected on the lessor's income statement. This reporting applies regardless of whether the lessor was primarily obligated to, or primarily benefitted from, the cost, and regardless of whether the lessor knows, can readily determine or can reliably estimate the amount of the cost paid by the lessee.
- If the lessor pays the third party, and therefore recovers the cost through payments it receives from the lessee (whether fixed or variable), the lessor will recognize the cost and the lessee's payments gross in the income statement (see the discussion that follows).

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Lessor applies the practical expedient

If the lessor applies the practical expedient and accounts for the lease and CAM as one operating lease component, the lessee's payments to reimburse the lessor for property taxes or insurance are accounted for as:

- fixed 'lease payments', if the reimbursement is structured as a fixed adjustment to the base lease payment (i.e. a gross lease); or
- variable lease payments, if the reimbursement varies based on the lessor's costs (i.e. a net lease).

Lessor does not elect the practical expedient or the lease and non-lease component(s) do not qualify for combination

If the lessor does not (or cannot) apply the practical expedient and the contract includes a lease component and non-lease component (e.g. CAM), the lessee's payments to reimburse the lessor for real estate taxes and insurance are allocated to the lease and non-lease components based on the transaction price allocation guidance in Topic 606. [842-30-25-11(b), 842,10,15-40, 842-10-55-141 – 55-142]

If the lessor structures the reimbursement through a fixed adjustment to the base lease payment (i.e. a gross lease), it would consider the adjustment part of the total consideration in the contract, similar to any other fixed lease payments. The lessor then allocates the total consideration in the contract to the lease component(s) and the non-lease component(s) and generally recognizes the amount allocated to the lease component(s) over the lease term(s) on a straight-line basis, while recognizing the amount allocated to the non-lease component(s) as those performance obligations are satisfied under Topic 606. This would apply even if the lessor itemized that portion of the fixed payment in the contract for reimbursement of taxes and insurance. [842-10-15-40, 842-10-55-143, 842-30-25-11]

If the reimbursement to the lessor varies based on the lessor's costs (i.e. a net lease), those variable payments generally will be partially attributed to the non-lease component(s) in a similar manner – i.e. based on the transaction price allocation guidance in Topic 606.

However, we believe a lessor must consider whether allocating (or not allocating) these amounts to a non-lease component (e.g. CAM) will result in allocations to the lease and non-lease components that no longer meet the Topic 606 allocation objective. For example, we believe it would be inappropriate for a lessor to allocate a portion of the property tax and insurance charges to CAM services if that allocation would result in reporting CAM income significantly greater than its stand-alone selling price. [606-10-32-28]

It may instead be the case that the lessee's reimbursements of lessor property tax and/or insurance costs should be allocated entirely to the lease component(s) based on the variable consideration allocation guidance in Topic 606. [606-10-32-40]

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question G22

If a lessor separates lease and non-lease components, how should it estimate the stand-alone selling price of CAM to allocate total consideration for an operating lease?

Interpretive response: Often CAM is the only non-lease component in a lease contract. While a lessor charges for CAM using a variety of mechanisms (e.g. maintenance cost reimbursement, incremental fixed payment, incremental but part of a single lease payment), the principle for determining the stand-alone selling price when the lessor is separating lease and non-lease components is the same. (See Question G20 for additional discussion about the practical expedient.) The lessor should apply the guidance in Topic 606 to estimate the price at which it would provide CAM separately.

While no entity may provide exactly the same services separately, we believe a lessor generally will be able to identify market data to support using an adjusted market assessment approach or an expected cost plus a margin approach. We generally do not believe it would be appropriate to use the residual approach to estimate the stand-alone selling price for CAM.

Additionally, we do not believe it would be appropriate for a lessor to use only the amount of actual costs billed to a lessee on a cost pass-through basis as the stand-alone selling price for CAM. If a vendor were to provide those services separately from a lease, the price it would charge a customer would include some amount of profit margin because a profit-oriented business would not perform services for no profit.

However, if the lessor bills to the lessee an administrative fee in addition to the actual costs incurred to provide CAM, the total billings may approximate the stand-alone selling price of CAM if the administrative fee added to the actual costs approximates the profit margin that the lessor would have charged had those services been provided separately. In that case, a lessor may be able to allocate those cost plus administrative fee billings entirely to CAM if that would result in an allocation to the lease and CAM that represents the relationship between the stand-alone selling prices of those two components. The lessor would not allocate those billings to both the lease and CAM. The lessor should consider all the relevant facts and circumstances in these situations. [606-10-32-28, 32-34, 32-40]

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question G23

If a lessor separates lease and non-lease components, should it allocate variable CAM charges entirely to the CAM non-lease component? Should a lessor allocate any of the fixed lease payment to the CAM non-lease component?

Interpretive response: It depends. Because lease contracts that include variable payments for CAM[17] services generally specify that those payments relate to the maintenance services, those payments would be included in the consideration in the contract. A lessor that separates lease and non-lease components allocates those payments entirely to the CAM non-lease component if this would result in an allocation to the lease and CAM that would be consistent with the allocation objective of Topic 606. (See Question G20 for additional discussion about the practical expedient.)

While allocating only the variable CAM charges to the non-lease component may not meet the allocation objective, allocating a portion of the fixed lease payment to the non-lease component when combined with the variable payments, may meet the allocation objective of Topic 606. The allocation objective would not be met when allocating only the variable CAM charges because those amounts are simply a pass-through of the lessor's costs. They do not include a profit margin and thus will not approximate stand-alone selling price as discussed in Question G22. Once the lessor allocates an amount to the CAM non-lease component, it may need to further allocate that amount to each distinct service period within a single CAM performance obligation as discussed in Question G24. [606-10-32-28 – 32-29, 32-39 – 32-40]

We believe there may be a number of acceptable methods for allocating the consideration in the contract (and changes to that consideration) to the lease and CAM components, particularly when there are variable payments. In evaluating its allocation methodology, we believe a lessor should focus on whether the resulting reported amounts allocated to each component meet Topic 606's allocation objective. That is, do the allocated amounts reasonably depict the amount of consideration to which the entity expects to be entitled in exchange for transferring each of the components (e.g. the lease and CAM).

For example, we believe it would be inappropriate for a lessor to allocate fixed or variable amounts between components in such a way that reported results for any of the individual components ultimately, after considering all the payment terms of the contract, differs significantly from the relative stand-alone selling price of that component. This means that a lessor must consider the result of its allocation on each of the identified components; it is not acceptable to conclude that an allocation is appropriate solely because it faithfully represents the amount to which the lessor expects to be entitled for providing one or some of the components of the contract. [606-10-32-28 – 32-29, 32-39 – 32-40]

---

[17] Lessors should be careful not to include reimbursements for real estate taxes and insurance in the variable payments allocated entirely to CAM. Real estate taxes and insurance reimbursements are not components in the contract and are not specifically related to CAM.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question G24

If a lessor separates a CAM non-lease component, how should it determine the number of performance obligations?

Interpretive response: The lessor should determine the number of performance obligations after allocating contract consideration to CAM as a non-lease component as discussed in Question G23. This assumes that the lessor has not elected, or does not qualify for, the non-separation practical expedient discussed in Question G20). The lessor will need to determine whether CAM comprises one or multiple performance obligations using the guidance on identifying performance obligations in Topic 606.

We believe the nature of CAM is such that it will frequently comprise only a single performance obligation under Topic 606 and, therefore, will be a single non-lease component when allocating the consideration in the contract under Topic 842. In many lease arrangements, CAM is substantially similar to the hotel management services in Example 12A in Topic 606 (see discussion in Question C30) and the IT outsourcing services example discussed by the Revenue Recognition Transition Resource Group at its July 2015 meeting. That is, in fulfilling its promise to provide CAM (i.e. to maintain the common areas of the multi-tenant property), the lessor performs a variety of underlying activities to fulfill that promise, and those activities vary in terms of timing and quantity.

For example, at lease commencement, it is not known how much snow the lessor will have to clear from the parking lot during the winter, the extent of landscaping that will be required during the spring and summer months, when or how often minor repairs will be needed or when unexpected janitorial needs will arise. Regardless, the lessor commits to undertaking those activities as needed to fulfill its overall promise to the lessee. [606-10-55-157B – 55-157E]

The preceding paragraph notwithstanding, the characterization of an activity as part of CAM does not necessarily mean it should not be a separate non-lease component. The lessor will need to evaluate each activity that is promised in the contract as part of CAM and potentially separately account for those that provide a different or incremental benefit to the lessee beyond maintaining the common areas of the property.

For example, the lessor will frequently provide the utilities needed by the lessee (e.g. heating, water, electricity). In some cases, the provision of utilities is characterized as part of, or will be billed together with, CAM. Despite its characterization in the contract or how it is billed, the provision of utilities to the lessee would generally be a separate non-lease component because the provision of utilities to the lessee's retail or office space is not an underlying activity to maintaining the common areas of the property.

While CAM, appropriately defined, will typically be a single, integrated performance obligation, entities may need to further consider whether that single, integrated performance obligation comprises a series of distinct CAM service periods (e.g. 36 distinct months of CAM). This conclusion may be important if all or a portion of the payments to which the lessor will be entitled for providing CAM are variable. If so, the lessor may, if the specified Topic 606 criteria are met, be required to allocate the variable payments to the distinct CAM service periods to which each variable payment relates – e.g. allocate the

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

variable CAM billing for Month 1 of the 36-month lease entirely to CAM services provided in Month 1 – rather than to the 36-month CAM performance obligation as a whole. Allocation to each distinct service period, rather than to the entire performance obligation, may affect the lessor's pattern of revenue recognition. [606-10-32-40]

Question G25

If a lessor separates a CAM non-lease component, how should it allocate variable CAM payments (and recognize revenue) when CAM is determined to be a series of distinct service periods?

Interpretive response: Any portion of the fixed payments in the contract that is allocated to CAM relates to its performance obligation as a whole and is recognized using a single measure of progress toward complete satisfaction of the performance obligation under Topic 606. This assumes that the lessor is not applying the non-separation practical expedient discussed in Question G20.

Meanwhile, a lessor will allocate variable payments that relate specifically to a distinct service period to that distinct period if that allocation meets Topic 606's allocation objective. For example, CAM billings that relate to the lessor's CAM activities performed in Month 1 of a 36-month CAM service period generally will be allocated entirely to Month 1. This is similar to the way a property manager would allocate management fees (see additional discussion in Questions E10 and F130).

Making this determination may frequently revolve around whether the lessor concludes that the total amount of revenue allocated to each distinct service period reasonably reflects the value of CAM services provided to the customer for that period. For example, a lessor may conclude this is the case if the amount(s) that will be allocated to each service period varies in reasonable proportion to the extent of the activities the lessor undertakes.

If the variable payments for CAM are not allocable to the distinct service periods within the larger performance obligation, those payments are estimated subject to the Topic 606 variable consideration constraint and allocated to the performance obligation as a whole consistent with the portion of the fixed payments allocated to CAM. Together those payments are recognized using a single measure of progress toward complete satisfaction of the performance obligation under Topic 606.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question G26

How should a lessor account for CAM provided in a lease after it adopts Topic 606 but before it adopts Topic 842?

Interpretive response:

Accounting for existing leases before the adoption of Topic 842

Topic 606 is a 'residual standard' in that it requires the application of other Topics **first** if those other Topics specify how to account for one or more parts of the contract. Topic 606 only applies to the parts of the contract that other Topics do not address. CAM expenditures are defined as 'executory costs', and accounted for as part of the lease, under Topic 840. Therefore, CAM is not governed by Topic 606 until an entity adopts Topic 842. That being said, after the adoption of Topic 606, we would not object to an entity either: [606-10-15-4]

- analogizing to the guidance in Topic 606 to determine the measure of progress to apply when recognizing CAM revenue; or
- separately presenting CAM revenues as non-lease or service revenue.

If a lessor decides to separately present CAM revenue as non-lease revenue, it is acceptable to allocate revenue between the lease and CAM using either: (1) the requirements in Topic 840 or (2) the transaction price allocation guidance in Topic 606. That separate presentation (if elected) should be reflected in the comparative periods presented, even if the lessor elects to use the effective date transition method to adopt Topic 842.

Topic 840 specifies that CAM is within its scope based on the following.

- It defines maintenance as an executory cost.
- It states that "if an arrangement contains a lease and related **executory costs** [emphasis added], as well as other non-lease elements, the classification, recognition, measurement, and disclosure requirements of this Topic shall be applied by both the purchaser and the supplier to the lease element of the arrangement."
- It characterizes related executory costs as part of 'those for the lease'. [840-10-25-1(d), 15-17, 15-19(a)]

Accounting for existing leases after the adoption of Topic 842

Assuming that lease classification is the same before and after adoption of Topic 842, the lessor will not reevaluate the identification of and allocation to lease and non-lease components. This applies unless the lease is modified on or after the effective date and that modification is not accounted for as a separate contract. The lessor will continue to account for CAM provided as part of the lease contract as it did before the effective date of Topic 842 (see above).

Accounting for leases that commence on or after the adoption of Topic 842

For all leases that commence on or after the adoption of Topic 842, the lessor will identify CAM as a non-lease component and account for it under Topic 606 if it does not elect the practical expedient discussed in Question G20.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Question G27

After adopting Topic 842, how should a lessor present in its income statement CAM revenue and lease income?

Interpretive response: If a lessor applies the practical expedient not to separate lease and non-lease components (see Question G20), we believe that **all** the income from the lease (including payments contractually identified as CAM, but accounted for as lease payments when the lessor applies the practical expedient) should be classified in the income statement in a single line item.

If a lessor is not applying the non-separation practical expedient, we believe a lessor may either:

- separate the lease income from CAM revenue; or
- present lease income and CAM revenue within the same line item in the income statement because Topics 606 and 842 do not require an entity to separately present income streams within their scopes.

However, SEC registrants are prohibited from combining revenue from services with income from rentals when either one is more than 10% of total sales and gross revenues. [Reg S-X Rule 5-03(b)]

Lessors that are not applying the non-separation practical expedient are reminded that Topics 606 and 842 require specific disclosures relative to transactions within their scopes. This means that CAM revenue and lease income generally will need to be presented separately in the notes to the financial statements even if they are not presented separately in the income statement. [606-10-50-4, 842-10-15-31]

Question G28

Is a lessor permitted to recast comparative periods to conform to its Topic 842 presentation of revenue from lease and qualifying non-lease components?

Interpretive response: The specific lease and non-lease components for which it would be acceptable for a lessor to recast its comparative period income statement presentation differ if the lessor is an SEC registrant.

Non-SEC registrants

Topic 842 does not apply to the comparative periods presented when using the effective date method. Therefore, Topic 250 should be considered.

We do not believe a change in income statement aggregation or disaggregation is a change in accounting principle under Topic 250 (see Question 3.5.10 of KPMG Handbook, Accounting changes and error corrections) if both the previous and the new aggregations are acceptable under the applicable US GAAP – i.e. Topic 840 in this instance. And because Topic 840 does not specify separate or combined income statement presentation for the revenue items

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

discussed in the background, we believe either was acceptable under Topic 840.

If a lessor changes its income statement aggregation for the comparative periods, the notes to the financial statements should disclose the change. We do not believe a preferability assessment under Topic 250 is required.

SEC registrants

We believe our response for non-SEC registrants also applies to SEC registrants if, and only if, the item presented separately from lease revenue was an executory cost element (e.g. maintenance, including CAM), rather than a non-lease element (i.e. goods or a substantial service), under Topic 840.

However, because of the guidance in SEC Regulation S-X applicable to SEC registrants, we do not believe income statement presentation of lease and non-lease goods or substantial service revenues on a combined basis was an acceptable accounting alternative for those lessors. Therefore, a lessor is not permitted to change its comparative period income statements to combine revenues from leases and non-lease goods or substantial services.

We do not believe lessee payments of executory costs were required to be presented separately from lease revenue under Regulation S-X because Topic 840 characterizes those payments as part of 'those for the lease'. Chapter 13A of KPMG Handbook, Leases, provides additional discussion for lessors using the effective date transition method.

Question G29

Is a lessor permitted to recast comparative periods to conform to its Topic 842 gross vs net presentation?

Background: As discussed in Question G20, some lessors may be required to change their presentation of lessor costs (e.g. property taxes) and lessee payments thereof on adoption of Topic 842 from how they presented those items historically under Topic 840. This may create noticeable differences between a lessor's adoption year and comparative period financial statements.

Topic 840 and SEC guidance

Topic 840 does not prescribe gross or net presentation for lessor costs such as property taxes or insurance or lessee payments thereof, and there is no relevant SEC guidance.

Interpretive response: It depends. While Topic 842 would generally not permit recasting the comparative periods, Topic 250 may provide an avenue to do so.

Topic 842 does not permit recasting the comparative periods because, under the effective date method, Topic 842 does not apply before the effective date – i.e. it does not apply to the comparative periods presented. Recasting the comparative periods to, for example, separately present previously netted income statement amounts would, in effect, be selectively applying the comparative period method to adopt the amendments in ASU 2018-20, while using the effective date method to adopt the remainder of Topic 842. [842-10-65-1(c)]

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Although Topic 842 does not apply to the comparative periods presented when using the effective date transition method, Topic 250 may be considered. A change in gross versus net income statement presentation is a change in accounting principle under Topic 250 (see section 3.3 of KPMG Handbook, Accounting changes and error corrections). And because Topic 840 does not prescribe gross or net income statement presentation for lessor costs and lessee payments thereof, a lessor may be able to justify a change to its comparative periods' gross versus net income statement presentation to conform to its post-effective date presentation as preferable. An entity's facts and circumstances will affect whether or not such a change is preferable, and whether a preferability determination is required for the change. [250-10-45-2 – 45-8]

Chapter 13A of KPMG Handbook, Leases, provides additional discussion for lessors using the effective date transition method.

Question G30

Does Subtopic 340-40 change whether an entity can capitalize costs incurred to sell real estate projects?

Interpretive response: Topic 340 supersedes the guidance in Subtopic 970-340 on accounting for costs incurred to sell real estate projects. Those costs generally will now be evaluated for capitalization using guidance on the incremental cost of obtaining a contract and costs to fulfill a contract. [340-40-25-1 – 25-8]

An incremental cost of obtaining a sales contract is a cost that would not have otherwise been incurred if the contract were not obtained. An entity capitalizes[18] those costs under Topic 340 if it expects to recover them. Costs that an entity would have incurred regardless of whether it obtained a sales contract are recognized under Topic 340 as an expense when incurred unless those costs are capitalizable under other guidance or explicitly chargeable to the customer regardless of whether a contract was obtained.

In many cases, the seller would have incurred indirect costs of obtaining a sales contract such as model units and their furnishings, sales facilities, legal fees for preparation of prospectuses and semi-permanent signs, regardless of whether the seller obtained a contract. The seller generally does not attribute these costs to a specific contract. As a result, the seller generally would expense these costs as incurred, unless they are within the scope of another topic – e.g. model units and sales facilities may be property, plant or equipment that are accounted for under Topic 360.

If the costs incurred to **fulfill** a sales contract are in the scope of other guidance, then the entity accounts for them using the other guidance (e.g. Topic 360). Otherwise, an entity recognizes an asset only if the costs:

[18] As a practical expedient, an entity may recognize the incremental cost of obtaining a contract as an expense when incurred if the amortization period of the asset that would have otherwise been recorded is one year or less.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

- relate directly to an existing contract or specific anticipated contract;
- generate or enhance resources of the entity that will be used to satisfy performance obligations in the future; and
- are expected to be recovered. [340-40-25-5]

The costs associated with model units and their furnishings, rental facilities, semi-permanent signs, grand openings and unused rental brochures are capitalized if they relate to, and their recovery is reasonably expected from, future rental operations and rental overhead is expensed as incurred. Topic 310 (receivables) defines initial direct costs and Subtopic 840-20 prescribes their accounting. [970-340-25-16 – 25-17]

As previously discussed, Topic 842[19] superseded Topic 840 in 2019 for calendar year-end public business entities and certain employee benefit plans and not-for-profit entities. It is effective for 2022 reporting periods for other calendar year-end entities. (For more information on Topic 842's effective date, see Question A30).

Topic 842 also amends Topic 310 to require that initial direct costs associated with leasing activities be accounted for under Topic 842. That standard defines initial direct costs as incremental costs of a lease that the lessor would not have incurred if it had not obtained the lease (e.g. commissions, payments made to an existing tenant to incentivize that tenant to terminate its lease).

The guidance excludes from the definition of initial direct costs those costs that the lessor would have incurred regardless of whether it obtained the lease. These exclusions include the costs to negotiate or arrange a lease, such as fixed employee salaries, general overhead, advertising, tax and legal advice, and evaluating a prospective lessee's financial condition. [842-10-30-9 – 30-10]

Only those costs that are considered initial direct costs are eligible for deferral and, if deferred, recognized over the lease term. Many of the costs incurred to rent real estate projects that are capitalized under Subtopic 970-340 (and some costs that currently are considered initial direct costs under Topic 310), are expensed as incurred when Topic 842 is adopted. [842-30-25-1(c), 25-8, 25-10]

---

[19] For more information on Topic 842, see Handbook, Leases.

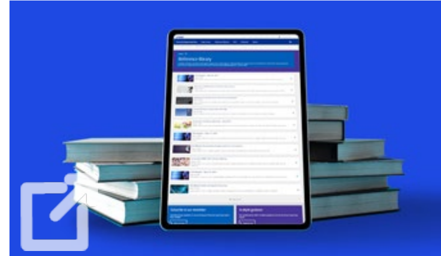
© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

KPMG Financial Reporting View

Delivering guidance and insights, KPMG Financial Reporting View is ready to inform your decision making. Stay up to date with us.

Defining Issues

Our collection of newsletters with insights and news about financial reporting and regulatory developments, including Quarterly Outlook and FRV Weekly.



Handbooks and Hot Topics

Our discussion and analysis of accounting topics – from short Hot Topics that deal with a topical issue, to our in-depth guides covering a broad area of accounting.

CPE opportunities

Register for live discussions of topical accounting and financial reporting issues. CPE-eligible replays also available.

Financial Reporting Podcasts

Tune in to hear KPMG professionals discuss major accounting and financial reporting developments.

Visit **Financial Reporting View**
and sign up for news and insights

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Access our US Handbooks

As part of Financial Reporting View, our library of in-depth guidance can be accessed here, including the following Handbooks.

- Accounting changes and error corrections
- Asset acquisitions
- Bankruptcies
- Business combinations
- Business combinations (SEC reporting)
- Climate risk in the financial statements
- Consolidation
- Credit impairment
- Debt and equity financing
- Derivatives and hedging
- Discontinued operations and held-for-sale disposal groups
- Earnings per share
- Employee benefits
- Equity method of accounting
- Fair value measurement
- Financial statement presentation
- Foreign currency
- GHG emissions reporting
- Going concern
- IFRS® compared to US GAAP
- Impairment of nonfinancial assets
- Income taxes
- Internal control over financial reporting
- Inventory
- Investments
- Leases
- Long-duration contracts
- Reference rate reform
- Research and development
- Revenue recognition
- Revenue: Real estate
- Revenue: Software and SaaS
- Segment reporting
- Service concession arrangements
- Share-based payment
- Software and website costs
- Statement of cash flows
- Tax credits
- Transfers and servicing of financial assets

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Acknowledgments

This edition of Questions and Answers has been produced by the Department of Professional Practice (DPP) of KPMG LLP in the United States.

We would like to acknowledge the efforts of the main contributors to the latest edition of this publication:

Mike Breen

Valarie Mosier

Ryan Campbell

We would also like to acknowledge the current and former members of DPP who contributed significantly to this Handbook: Richard Binderup, Kimber Bascom, Nick Burgmeier, Sam Hall, Brandon Kano, Kevin Manson, Bob Mosier, Scott Muir, Angie Storm and Kirby Vilker.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

Learn about us: **kpmg.com**

The FASB *Accounting Standards Codification*® material is copyrighted by the Financial Accounting Foundation, Norwalk, Connecticut.

© 2024 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. USCS013296-1A

The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization.

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.

This publication contains copyright © material of the IFRS® Foundation. All rights reserved. Reproduced by KPMG LLP with the permission of the IFRS Foundation. Reproduction and use rights are strictly limited. For more information about the IFRS Foundation and rights to use its material please visit www.ifrs.org.

Disclaimer: To the extent permitted by applicable law the IASB, the ISSB and the IFRS Foundation expressly disclaims all liability howsoever arising from this publication or any translation thereof whether in contract, tort or otherwise (including, but not limited to, liability for any negligent act or omission) to any person in respect of any claims or losses of any nature including direct, indirect, incidental or consequential loss, punitive damages, penalties or costs.

Information contained in this publication does not constitute advice and should not be substituted for the services of an appropriately qualified professional.

'ISSB™' is a Trade Mark and 'IFRS®', 'IASB®', 'IFRIC®', 'IFRS for SMEs®', 'IAS®' and 'SIC®' are registered Trade Marks of the IFRS Foundation and are used by KPMG LLP under licence subject to the terms and conditions contained therein. Please contact the IFRS Foundation for details of countries where its Trade Marks are in use and/or have been registered.