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ASC 606 CONSIDERATIONS
for Life Sciences and Medical Device Companies

STEP ONE: IDENTIFY THE CONTRACT

☐ Evaluate the contract and verify that it creates a customer-vendor relationship and not a collaborative partnership relationship.

☐ Wholesalers that receive product shipments are generally considered the ASC 606 customer.

☐ A pricing arrangement with indirect customers (such as a buying organization, pharmacy chain, or hospital) usually does not create an ASC 606 contract.

☐ An ASC 606 'contract' must be collectible. Consider a customer's ability and willingness to pay, especially for new and less stable customers. A letter of credit or third party's guarantee could offset this risk.

EXAMPLE: The collectability of revenues after concessions must be evaluated upfront when exporting product to a new foreign customer with high sovereignty risk.

STEP TWO: IDENTIFY THE PERFORMANCE OBLIGATIONS

☐ Review contract terms for ASC 606 implications, particularly custom arrangements for significant customers.

☐ Assess if multiple goods and services in an arrangement constitute a single or multiple performance obligations.

EXAMPLE: A licensing contract includes other services (for example, R&D and/or manufacturing). The license and each of the services must be evaluated to determine if there is one performance obligation or several.

EXAMPLE: Medical device company transferring equipment with consumables and installation

☐ Free goods or services, if material at the contract level, would be a separate performance obligation.

☐ Review customer options for additional products or services as they may be deemed to be a separate performance obligation.

EXAMPLE: A license includes an option for an additional therapeutic indication.

STEP THREE: DETERMINE THE TRANSACTION PRICE

☐ Good-quality estimates of probable variable consideration (such as chargebacks, price protection, commercial and government rebates, sales discounts) are included.

☐ Gross to net deductions are not expected to change under ASC 606 for both branded and generic companies.

☐ Rights of return for product sales would not limit estimating the transaction price, however they must be estimated and recognized in the total transaction price. Therefore, sales could be recorded earlier under ASC 606, which are presently deferred under legacy GAAP.

☐ Variable consideration containing a high degree of uncertainty (for example, milestone payments upon FDA approval of a drug) is not included in the transaction price.

☐ Sales-and usage-based royalties are excluded, and recorded coinciding with the actual period of sale or usage without any lag in Step 5. However, minimum guaranteed royalties are included in the total transaction price in Step 3.

STEP FOUR: ALLOCATE THE TOTAL TRANSACTION PRICE TO ALL THE PERFORMANCE OBLIGATIONS

☐ This step only applies if there is more than 1 performance obligation .

☐ Develop good quality standalone selling prices if quoted prices are not available.

EXAMPLE: A medical device company supplies equipment, consumables, and training/installation services. Each of these is deemed to be a separate performance obligation. The company will allocate the total transaction price proportionally based on the relative standalone selling price of the individual performance obligations.

STEP FIVE: RECOGNIZE REVENUE AS THE CUSTOMER ACHIEVES CONTROL OF THE GOODS OR SERVICES

☐ Revenues arising from 'functional' licenses of intellectual property (for example, drug formulas) are recognized entirely at inception. 'Symbolic' license revenues (for example, logos or brand names) are recognized over the license term.

☐ In a sell through model, evaluate when ASC 606 'control' of the product is transferred to the customer. Based on this assessment, revenue may be recognized earlier under ASC 606 than under current guidance.

☐ In arrangements with FOB shipping point terms (wherein transit losses are borne by the customer), determine when ASC 606 'control' of the goods has truly passed to the customer.

☐ Since returned drugs from customers are not generally resold in the life sciences industry, do not record an asset for expected returned inventory.

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