

## Financial Reporting Center – Revenue Recognition

### Working Draft: Health Care Entities Revenue Recognition Implementation Issue



**Issue #8-3**– Application of FASB ASC 606, *Revenue from Contracts with Customers*, to Continuing Care Retirement Community Contracts

**Expected Overall Level of Impact to Industry Accounting:** Significant

**Wording to be Included in the Revenue Recognition Guide:**

#### *Background*

1. Continuing care retirement communities (CCRCs) provide residents with a diversity of residential, social, and health care services, in accordance with a resident service agreement (resident agreement or contract) specifying the obligations of the CCRC to the resident. Generally, a resident entering a CCRC initially lives in an independent living unit designed for seniors such as a cottage, duplex, townhome, or apartment. If and when the health of a resident declines, he or she may be permanently transferred to an assisted living facility or a nursing facility, both of which are generally located on the same campus as the independent living units. The health care services provided by CCRCs generally include nursing care and assisted living, and may also include home health care, physician services, and other health care related services. These health care services are provided in addition to the residential services and amenities, including social, recreational, dining, and laundry services. In addition to providing these services to CCRC residents, certain services, predominantly assisted living and nursing services, may be provided to nonresidents. Most CCRCs require some type of entrance (or advance) fee, which may or may not be refundable, and a monthly fee. The entrance fee and monthly fee may vary depending on the type of contract selected by the resident.
2. This paper is focused on Type A life care contracts that are all-inclusive continuing-care contracts that include residential facilities, other amenities, and access to health care services, primarily assisted living and nursing care, for little or no increase in periodic (or monthly) fees, other than increases as stipulated in the resident agreement, generally based on increases in operating costs or inflationary increases. CCRCs should separately assess other types of life care contracts to determine the appropriate accounting under FASB ASC 606, *Revenue from Contracts with Customers*.

### *Initial Recognition*

3. At inception of a CCRC contract (that is, a contract between the CCRC and a new resident), the CCRC is required to apply the guidance in FASB ASC 606 to determine how revenue should be recognized over the term of the contract, based on allocating the contract's transaction price among the distinct goods or services (performance obligations) promised in the contract.

### *Identifying the Contract With a Resident*

4. Generally, each resident enters into a written resident agreement with the CCRC. This agreement establishes the rights and obligations of both the CCRC and the resident. A potential resident must apply for entrance to the CCRC, with the application process generally considering, among other things, health status and financial resources. Payment terms are clearly outlined in the resident agreement, with entrance fees paid at the inception of the contract and periodic fees paid monthly. Given the financial screening process for residents, CCRCs generally do not have collectability issues; however, collectability is still required to be assessed in accordance with FASB ASC 606-10-25-1(e). FinREC believes a resident agreement between the resident and the CCRC would generally meet the criteria in FASB ASC 606-10-25-1 to be considered a contract with a customer to be accounted for under FASB ASC 606.
5. Type A life care contracts (or resident agreements) generally contain two payment sources—the entrance fee and the monthly fees. The entrance fee is a fixed amount paid at the time the contract is signed and the resident takes occupancy. It may be fully refundable, fully nonrefundable, or a combination of both. Refundable entrance fees are those entrance fees that are guaranteed to be refunded regardless of when the contract is terminated. Nonrefundable entrance fees are those entrance fees that are either nonrefundable at contract inception or are refundable on a decreasing basis for a fixed period of time (for example, ratably over 48 months), at which point the entrance fees become nonrefundable.
6. Under a Type A life care contract, in exchange for an entrance fee and a monthly fee that will not increase as long as the resident resides at the CCRC (other than for potential inflationary increases), the resident has the right to initially occupy an independent living unit at the CCRC and continue to live in that unit or occupy an assisted living unit or skilled nursing bed at the CCRC when the resident needs health care services. The resident also has the right to move out and discontinue paying the monthly fee at any time; however, that resident would generally forfeit—and not receive future value for—at least a portion of the nonrefundable entrance fee paid at the inception of his or her contract upon vacating the CCRC.
7. Because a CCRC resident has the ability to move out and discontinue paying the monthly fee at any time, FinREC believes the resident agreement for a Type A life care CCRC resident is generally a monthly contract with the option to renew.
8. CCRCs should consider whether the Type A life care contract contains a lease in the scope of FASB ASC 840, *Leases* (or FASB ASC 842, *Leases*, after adoption of that Topic). If it is determined that the Type A life care contract contains a lease, the guidance in FASB ASC 606-10-15-4 should be applied to separate the elements that should be accounted for under FASB ASC 840 (or FASB ASC 842 after adoption) and FASB ASC 606.

### *Identifying the Performance Obligations in the Contract*

9. Paragraphs 14–22 of FASB ASC 606-10-25 discuss how to determine whether promised goods and services in the contract represent performance obligations.
10. FASB ASC 606-10-25-14 establishes that a CCRC should assess goods or services promised in a contract and identify as performance obligations each promise to transfer to the resident either:
  - a. A good or service (or bundle of goods or services) that is distinct; or

- b. A series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.

11. FASB ASC 606-10-25-18 states,

Depending on the contract, promised goods or services may include, but are not limited to, the following:

...

- e. Providing a service of standing ready to provide goods or services (for example, unspecified updates to software that are provided on a when-and-if-available basis) or of making goods or services available for a customer to use as and when the customer decides.

12. The typical resident agreement for a Type A life care resident provides that the resident can live in the CCRC and access health care as needed for little or no increase in periodic fees other than increases as stipulated in the resident agreement, generally based on increases in operating costs or inflationary increases. The goods and services a resident will receive under the resident agreement are dependent on the resident's health and life span along with his or her decision to continue to reside at the CCRC.

13. FinREC believes that the promised good or service (that is, the performance obligation) in the resident agreement for a Type A life care resident is that the CCRC is standing ready each month to provide a service such that the resident can continue to live in the CCRC and access the appropriate level of care based on his or her needs. Other goods or services offered separately by the CCRC that are not included in the monthly fees should also be assessed to determine if any additional performance obligations exist.

14. Paragraphs 42–43 of FASB ASC 606-10-55 state:

If, in a contract, an entity grants a customer the option to acquire additional goods or services, that option gives rise to a performance obligation in the contract only if the option provides a material right to the customer that it would not receive without entering into that contract (for example, a discount that is incremental to the range of discounts typically given for those goods or services to that class of customer in that geographical area or market). If the option provides a material right to the customer, the customer in effect pays the entity in advance for future goods or services, and the entity recognizes revenue when those future goods or services are transferred or when the option expires.

If a customer has the option to acquire an additional good or service at a price that would reflect the standalone selling price for that good or service, that option does not provide the customer with a material right even if the option can be exercised only by entering into a previous contract. In those cases, the entity has made a marketing offer that it should account for in accordance with the guidance in this Topic only when the customer exercises the option to purchase the additional goods or services.

15. Paragraph 11 of TRG Agenda Ref. 54, "Considering Class of Customer When Evaluating Whether a Customer Option Gives Rise to a Material Right," notes that paragraph BC386 of FASB Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, explains that the purpose of the guidance in paragraphs 606-10-55-42 through 55-43 is to distinguish between:

- a. an option that the customer pays for as part of an *existing* contract (that is, a customer pays in advance for future goods or services), and
- b. a marketing or promotional offer that the customer did not pay for and, although made at the time of entering into a contract, is not part of the contract (that is, an effort by an entity to obtain *future* contracts with a customer).

16. Paragraph 12 of TRG Agenda Ref. 54 also explains, "Stated differently, the guidance in paragraphs 606-10-55-42 through 55-43 is intended to make clear that customer options that would exist independently of an existing contract with a customer do not constitute performance obligations in that existing contract."

17. FinREC believes that the nonrefundable entrance fee paid by a resident under a Type A life care contract contains a material right because, in effect, the resident is paying the CCRC in advance for future goods or services as explained in FASB ASC 606-10-55-42.
18. CCRCs should also evaluate whether the monthly renewal options included in the resident agreement for a Type A life care resident provide a material right to the resident. Consistent with the discussion in TRG Agenda Ref. 54, this evaluation will require judgment and should compare the monthly renewal option with what is offered to other new life care customers (that would be considered in the same class of customer), not what is offered to potential customers that would purchase services separately (on a fee-for-service basis). Generally, the monthly fees paid by a new life care customer would be comparable to the monthly fees paid by existing life care customers but individual facts and circumstances should be evaluated. As such, FinREC believes that generally, the monthly renewal options included in the resident agreement for a Type A life care resident would not provide a material right to the resident, in addition to the material right provided by the nonrefundable entrance fee, when comparing renewal options available to other life care customers. However, the facts and circumstances of each arrangement should be considered.

### *Determining the Transaction Price*

#### Monthly Fees

19. For Type A life care residents, monthly fees are specified in the resident agreement and are generally fixed with periodic changes based on increases for inflation or in operating costs, or other factors defined in the resident agreement. The monthly fees entitle the residents to the use of the residential facilities and other amenities, as well as access to health care services. As such, the monthly fees are included in the transaction price as the monthly options to extend the contract term are exercised.

#### Nonrefundable Entrance (Advance) Fees

20. Nonrefundable entrance fees are also specified in the resident agreement and are either nonrefundable at contract inception or are refundable on a decreasing basis for a fixed period of time, at which point the entrance fees become nonrefundable. For Type A life care residents, the nonrefundable entrance fee generally entitles the resident to the use of the residential facilities and other amenities, as well as access to health care services. As such, the nonrefundable entrance fees are a component of the transaction price.

#### Refundable Entrance (Advance) Fees

21. Refundable entrance fees are those entrance fees that are guaranteed to be refunded regardless of when the contract is terminated.
22. In accordance with FASB ASC 606-10-32-10, consideration received from a customer should be recognized as a liability if the entity expects to refund some or all of that consideration to the customer and is measured at the amount to which the entity does not expect to be entitled (that is, amounts not included in the transaction price). CCRCs are contractually obligated to refund the refundable entrance fees received from residents. As such in accordance with FASB ASC 606-10-32-10, FinREC believes that the refundable entrance fees received from residents should be recorded as a liability at the inception of the resident agreement and not included in the transaction price, because the CCRC expects to refund these amounts when the resident agreement is terminated.

### *Significant Financing Component*

#### Assessing Significance

23. FASB ASC 606 requires CCRCs to evaluate whether each of their contractual arrangements with residents provide a significant benefit of financing to either party of the contract. The financing component may be explicitly identified in the contract or, as frequently occurs in this industry, may be implied by payment terms of the contract.

24. FASB ASC 606-10-32-15 states, “an entity shall adjust the promised amount of consideration for the effects of the time value of money if the timing of payments agreed to by the parties to the contract (either explicitly or implicitly) provides the customer or the entity with a significant benefit of financing the transfer of goods or services to the customer.”
25. As a first step, it is important that the CCRC determine the level at which significance is required to be assessed. Paragraph BC234 of FASB ASU No. 2014-09 states, in part:

The Boards clarified that an entity should only consider the *significance* of a financing component at a contract level rather than consider whether the financing is *material* at a portfolio level. The Boards decided that it would have been unduly burdensome to require an entity to account for a financing component if the effects of the financing component were not material to the individual contract, but the combined effects for a portfolio of similar contracts were material to the entity as a whole.

26. The assessment of *significance* requires the CCRC to apply judgment. Paragraph BC234 of FASB ASU No. 2014-09 states, “that for many contracts, an entity will not need to adjust the promised amount of customer consideration because the effects of the financing component will not materially change the amount of revenue that should be recognized in relation to a contract with a customer.”
27. The assessment of significance is based upon individual facts and circumstances for each CCRC.

#### Entrance (Advance) Fees

28. Paragraphs BC237–BC238 of FASB ASU No. 2014-09 explain that FASB ASC 606 does not include an exemption for advance payments, as there may be situations when a significant financing component is present and to ignore the impact would likely skew the amount and pattern of revenue recognition. As such, an evaluation of whether entrance fees are deemed to have a significant financing component must be made. Such evaluations should be made based on the provisions of each resident contract.
29. CCRC contracts generally do not address the specific use of the entrance fees by the CCRC. As such, CCRCs utilize entrance fees for various purposes: working capital (that is, provision of services to residents), capital expenditures (including expenditures related to new buildings), refunds of entrance fee amounts due to prior residents, etc.
30. As indicated in paragraph 22, FinREC believes that the refundable entrance fees received by a CCRC from residents are not part of the transaction price. As a result, refundable entrance fees do not need to be considered in a CCRCs significant financing component analysis.
31. A CCRC should consider all facts and circumstances in assessing whether the nonrefundable entrance fee payment from a resident results in a contract that is deemed to have a significant financing component, including the impact of pricing options (entrance fees vs. monthly fees) presented to potential residents.
32. Paragraph BC232(b) of FASB ASU No. 2014-09 explains that “...An entity should consider the combined effect of: (1) the expected length of time between when the entity transfers the promised goods or services to the customer and when the customer pays for those goods or services; and (2) the prevailing interest rates in the relevant market. Although the Boards decided that the difference in timing between the transfer of goods and services and payment for those goods and services is not determinative, the combined effect of timing and the prevailing interest rates may provide a strong indication that a significant benefit of financing is being provided.”
33. FASB ASC 606-10-32-17 states, “Notwithstanding the assessment in paragraph 606-10-32-16, a contract with a customer would not have a significant financing component if any of the following factors exist:
- a. The customer paid for the goods or services in advance, and the timing of the transfer of those goods or services is at the discretion of the customer...”

A CCRC should determine whether the timing of the transfer of goods and services (for example, health care) under a CCRC contract are at the discretion of the resident in determining whether the transaction price under the CCRC contract contains a significant financing component.

34. Paragraph BC233(c) of FASB ASU No. 2014-09 states, in part, “In some circumstances, a payment in advance or in arrears in accordance with the typical payment terms of an industry or jurisdiction may have a primary purpose other than financing.... The primary purpose of those payment terms may be to provide the customer with assurance that the entity will complete its obligations satisfactorily under the contract, rather than to provide financing to the customer or the entity, respectively.”
35. Seniors choose to move into a CCRC primarily for the security that a CCRC provides, which includes the availability of health care in the future if needed. The payment of the entrance fee provides a resident with assurance that the CCRC will provide the goods and services that have been promised under the terms of the contract. The provision of this assurance by the CCRC should be considered when determining whether a nonrefundable entrance fee arrangement contains a significant financing component. The assessment of whether a nonrefundable entrance fee arrangement contains a significant financing component requires judgement and will be based upon individual facts and circumstances for each entity.
36. If a CCRC deems a nonrefundable entrance fee arrangement to contain a financing component, a CCRC should apply judgment to determine whether the financing component will materially change the amount of revenue that should be recognized in relation to a contract with a customer (that is, it is a significant financing component). The assessment of what constitutes significant will be based upon individual facts and circumstances for each entity. If an entity concludes the financing component is not significant, the entity does not need to apply the provisions of paragraphs 15–30 of FASB ASC 606-10-32 and adjust the consideration promised in determining the transaction price.

#### Discount Rate

37. FASB ASC 606-10-32-19 states, “After contract inception, an entity shall not update the discount rate for changes in interest rates or other circumstances (such as a change in the assessment of the customer’s credit risk).”
38. In accordance with FASB ASC 606-10-32-19, once a CCRC determines that a significant financing component is present and adjusts the promised consideration accordingly, the entity would continue to use the same assumed discount rate for the specific contract assessed unless there is a contract modification that results in the original contract being effectively terminated.

#### *Recognize Revenue When (or as) the Entity Satisfies a Performance Obligation*

#### Monthly Fee

39. As explained in paragraph 18, FinREC believes that generally, the resident agreement for a Type A life care resident is a monthly contract with options to renew, and the options to renew generally would not provide a material right to the resident. In accordance with FASB ASC 606-10-55-43, the options to renew should be accounted for only when the resident exercises the options.
40. FinREC believes that generally, the CCRC should recognize monthly fees as revenue when the services for the month are performed (that is, the CCRC satisfies the performance obligation).

#### Nonrefundable Entrance Fee

41. In accordance with paragraphs 42 and 51 of FASB ASC 606-10-55, the CCRC should recognize revenue for the material right associated with access to future services, when those future goods or services are transferred. Judgment is required to determine how to account for the nonrefundable entrance fee. FinREC believes that the nonrefundable entrance fee that contains a material right associated with access to future services (calculated

after consideration of any significant financing components as described in paragraphs 23–38), should be allocated to optional future periods covering a resident’s life expectancy.

42. FinREC believes one appropriate method to allocate the nonrefundable upfront fees to the material rights is a time-based measurement that results in an equal amount allocated to each month given the nature of the entity’s performance is that of having the various residential, social, or health care services available to the customer on a when-and-if needed basis each month for as long as the customer remains in the facility. A sample calculation using a time-based measure is included in Illustration 1, “Example of Single Resident — Type A or “Life Care” Contract: Time-Based.”
43. FinREC believes that another acceptable approach to allocate the nonrefundable upfront fees to the material rights based on when the future estimated costs or services are transferred to a CCRC resident (similar to a cost-to-cost method). A sample calculation using the cost-to-cost method is included in Illustration 2, “Example of Single Resident — Type A or “Life Care” Contract: Cost to Cost.”
44. FinREC believes that it would also be acceptable to apply the practical alternative to estimating the standalone selling price of the material right, as described in FASB ASC 606-10-55-45. Under this approach, the CCRC would allocate the transaction price to the optional periods by reference to the goods or services expected to be provided and the corresponding expected consideration for those future goods or services (for example, the monthly fees). This approach is illustrated in Example 51, “Option That Provides the Customer With a Material Right (Renewal Option),” of FASB ASC 606.

#### Portfolio Approach

45. The guidance in FASB ASC 606 specifies the accounting for an individual contract with a customer. Entities may use a portfolio approach as a practical expedient to account for contracts with customers as a group rather than individually, if as required in FASB ASC 606-10-10-4, the financial statement effects are not expected to materially differ from an individual contract approach.
46. If the CCRC reasonably expects that a portfolio approach would result in recognizing revenue that is not materially different than recognizing revenue on an individual contract basis, it is important for the CCRC to determine, based on the profile of its community, if it has one or multiple portfolios. If residents entering the CCRC are in a similar age cohort and health condition, then one portfolio may be considered. If there are variations in the age cohorts or other factors, then the CCRC might consider utilizing multiple portfolios.

#### Subsequent to Initial Recognition

47. For Type A life care contracts, assuming the CCRC allocates and recognizes the nonrefundable entrance fee as each month of services are transferred using either a time based or the cost-to-cost (or other appropriate) allocation method, there will be a contract liability balance that will decrease each period based on the amount of the nonrefundable up-front fee allocated to that period.
48. A CCRC may need to consider updating relevant assumptions at the end of each reporting period if the updates would have a material effect on the determination of revenue recognized during each reporting period. For example, life expectancies may change or, for the cost-to-cost method described in paragraph 43, the amount of time to be spent by a resident in each level of care that was estimated at contract inception, may change. CCRCs should apply judgment to determine the appropriate accounting for a change in an assumption that could impact the amortization of the contract liability balance (the nonrefundable entrance fees).
49. As documented in paragraph 11 of TRG Agenda Ref. No. 34, “March 2015 Meeting – Summary of Issues Discussed and Next Steps, related to Issue 1 in TRG Agenda Ref. No. 32: Accounting for a Customer’s Exercise of a Material Right,” one acceptable approach is for the exercise of a material right to be accounted for as a contract modification as the additional consideration received and/or the additional goods or services provided when a customer exercises a material right represent a change in the scope and/or price of a contract.

50. As discussed in paragraph 17, FinREC believes that the nonrefundable entrance fee paid by a resident under a Type A life care contract creates material rights for access to future services. In accordance with the discussion in TRG Agenda Ref. No. 34, one approach is to account for the exercise of the material rights by the customer as contract modifications. If the CCRC accounts for the exercise of the material rights as contract modifications, the guidance in FASB ASC 606-10-25-13(a) would apply and the changes in estimates, such as life expectancy or time spent at each level of care, would be accounted for prospectively.
51. A sample calculation reflecting a revised cost-to-cost methodology as a result of a resident transferring to another level of care earlier than projected at contract inception is included in Example 3.
52. It is unlikely that the terms of the CCRC resident agreement would be modified after inception; thus, the contract modification provisions in FASB ASC 606 are not discussed herein. However, if a contract were to be modified after inception, paragraphs 10–13 of FASB ASC 606-10-25 provide guidance for CCRCs to consider.

#### *Calculation of Obligation to Provide Future Services and Use of Facilities*

53. FASB ASC 606 does not change the guidance in sections 25 and 35 of FASB ASC 954-440 relating to the calculation of a CCRC onerous contract obligation to provide future services and use of facilities to current residents (the FSO Calculation). However, the determination of two components of the FSO Calculation may change as a result of applying FASB ASC 606. These two components are as follows:
- a. *Unamortized deferred revenue (contract liability)*—As discussed in paragraphs 41–44, there may be several acceptable approaches for recognizing the material right resulting from the nonrefundable entrance fees. CCRCs should be aware that FASB ASC 606 has superseded the guidance in FASB ASC 954-605-25-2 and FASB ASC 954-430-35-1, which may result in a different unamortized deferred revenue (contract liability) to be included in the FSO Calculation.
  - b. *Unamortized costs of acquiring initial contracts*—Issue No. 8-7, *Accounting for Contract Costs*, discusses application of the guidance in FASB ASC 340-40 to CCRCs. CCRCs should evaluate costs associated with acquiring new CCRC resident contracts to determine if these costs meet the requirements for capitalization as an asset under paragraphs 1–3 of FASB ASC 340-40-25. CCRCs should be aware that FASB ASC 340-40 has superseded the guidance in FASB ASC 954-720-25-7.

The illustrative example in FASB ASC 954-440-55-1 has been amended by FASB ASC 606 to reflect the change in terminology used to describe the two components above.

#### *Examples*

54. The following examples are illustrations of calculations for allocating the nonrefundable upfront fees to the material right provided to the Type A life resident. The actual pattern of revenue recognition should be based on the facts and circumstances of a CCRC's specific situation.



## Example 1

### Single Resident—Type A or "Life Care" Contract: Time Based

#### Assumptions:

Nonrefundable entrance fee	\$ 200,000
Life expectancy at move-in	14
Resident expires in year 7	

#### Allocation of nonrefundable entrance fee

	Life Expectancy (a)	Revenue Recognized	Contract Liability
Inception			\$ 200,000
Year 1	14.0	\$ 14,290	185,710
Year 2	13.4	13,860	171,850
Year 3	12.7	13,530	158,320
Year 4	12.1	12,080	145,240
Year 5	11.5	12,630	132,610
Year 6	10.9	12,170	120,440
Year 7	10.4	120,440	-
		\$ 200,000	

- (a) Facility determines its appropriate to update life expectancies each reporting period, based on actuarially determined life expectancies, using a prospective approach.

## Example 2

### Single Resident—Type A or "Life Care" Contract: Cost to Cost

#### Assumptions:

Non-refundable entrance fee	\$ 200,000
Inflation factor	3.00%
Expected years in IL	10
Expected years in Assisted Living (AL)	2
Expected years in Skilled Nursing (SN)	2

Estimated annual costs by level of care at contract inception:

IL	\$ 20,000
AL	\$ 40,000
SN	\$ 100,000

#### Calculations at Contract Inception:

##### *Projected Costs by Level of Care*

	IL	AL	SN
Year 1	\$ 20,000	\$ 40,000	\$ 100,000
Year 2	20,600	41,200	103,000
Year 3	21,218	42,436	106,090
Year 4	21,855	43,709	109,273
Year 5	22,511	45,020	112,551
Year 6	23,186	46,371	115,928
Year 7	23,882	47,762	119,406
Year 8	24,598	49,195	122,988
Year 9	25,336	50,671	126,678
Year 10	26,096	52,191	130,478
Year 11	26,879	53,757	134,392
Year 12	27,685	55,370	138,424
Year 13	28,516	57,031	142,577
Year 14	29,371	58,742	146,854

**Projected Costs by Level of Care for Sample Resident**

	IL	AL	SN	Total
Year 1	\$ 20,000	\$ -	\$ -	\$ 20,000
Year 2	20,600	-	-	20,600
Year 3	21,218	-	-	21,218
Year 4	21,855	-	-	21,855
Year 5	22,511	-	-	22,511
Year 6	23,186	-	-	23,186
Year 7	23,882	-	-	23,882
Year 8	24,598	-	-	24,598
Year 9	25,336	-	-	25,336
Year 10	26,096	-	-	26,096
Year 11	-	53,757	-	53,757
Year 12	-	55,370	-	55,370
Year 13	-	-	142,577	142,577
Year 14	-	-	146,854	146,854
<b>Totals</b>	<b>\$ 229,282</b>	<b>\$ 109,127</b>	<b>\$ 289,431</b>	<b>\$ 627,840</b>
<b>Relative values</b>	<b>36.52%</b>	<b>17.38%</b>	<b>46.10%</b>	<b>100.00%</b>

Note: Inflation factor of 3% applied to costs in all levels of care.

**Allocation of Nonrefundable Entrance Fee to Level of Care Based on Cost**

	IL	AL	SN	Total
Nonrefundable entrance fee	\$ 200,000	\$ 200,000	\$ 200,000	\$ 200,000
Relative value	36.52%	17.38%	46.10%	100.00%
Allocation	\$ 73,040	\$ 34,760	\$ 92,200	\$ 200,000

**Revenue Recognition Over Pattern of Transfer**

	Revenue Recognized (a)	Contract Liability (b)
Inception		\$ 200,000
IL:		
Year 1	\$ 6,370	193,630
Year 2	6,560	187,070
Year 3	6,760	180,310
Year 4	6,960	173,350
Year 5	7,170	166,180
Year 6	7,390	158,790
Year 7	7,610	151,180
Year 8	7,840	143,340
Year 9	8,070	135,270
Year 10	8,310	126,960
	<u>73,040</u>	
AL:		
Year 11	17,120	109,840
Year 12	<u>17,640</u>	92,200
	<u>34,760</u>	
SN:		
Year 13	45,420	46,780
Year 14	<u>46,780</u>	-
	<u>92,200</u>	
Total	<u><u>\$ 200,000</u></u>	

(a) Nonrefundable entrance fee allocated to optional periods using cost to cost measurement approach.

(b) Contract liability is equal to the nonrefundable entrance fee less revenue recognized.

**Example 3**

**Single Resident—Type A or "Life Care" Contract - Cost to Cost**

**Resident Moves to AL at Beginning of Year 7**

Contract liability at end of year 6	\$ 158,790
Inflation factor	3.00%
Expected years in Assisted Living (AL)	2
Expected years in Skilled Nursing (SN)	2

Estimated annual costs by level of care at contract inception:

AL	\$ 40,000
SN	\$ 100,000

**Calculations at Beginning of Year 7**

***Projected Costs by Level of Care for Sample Resident***

	IL	AL	SN	Total
Year 7	\$ -	\$ 47,762	\$ -	\$ 47,762
Year 8	-	49,195	-	49,195
Year 9	-	-	126,678	126,678
Year 10	-	-	130,478	130,478
Totals	<u>\$ -</u>	<u>\$ 96,957</u>	<u>\$ 257,156</u>	<u>\$ 354,113</u>
Relative values	<u>0.00%</u>	<u>27.38%</u>	<u>72.62%</u>	<u>100.00%</u>

Note: Inflation factor of 3% applied to costs in all levels of care.

***Allocation of Nonrefundable Entrance Fee to Level of Care Based on Cost***

	IL	AL	SN	Total
Transaction Price	\$ 158,790	\$ 158,790	\$ 158,790	\$ 158,790
Relative value	0.00%	27.38%	72.62%	100.00%
Allocation	<u>\$ -</u>	<u>\$ 43,480</u>	<u>\$ 115,310</u>	<u>\$ 158,790</u>

## Revenue Recognition Over Pattern of Transfer

	Revenue Recognized (a)	Contract Liability (b)
End of Year 6		\$ 158,790
AL:		
Year 7	\$ 21,420	137,370
Year 8	<u>22,060</u>	115,310
	<u>43,480</u>	
SN:		
Year 9	56,800	58,510
Year 10	<u>58,510</u>	-
	<u>115,310</u>	
Total	<u><u>\$ 158,790</u></u>	

- (a) Contract liability allocated to remaining optional periods using cost to cost measurement approach.
- (b) Contract liability is equal to beginning contract liability less revenue recognized.

Comments should be received by April 2, 2018, and sent by electronic mail to Andy Mrakovcic at [Andy.Mrakovcic@aicpa-cima.com](mailto:Andy.Mrakovcic@aicpa-cima.com), or you can send them by mail to Andy Mrakovcic, AICPA, 1211 Avenue of the Americas, NY 10036.