

## CBIZ, INC. AND SUBSIDIARIES

### NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (continued)

reclassified to interest expense in the same period during which the hedged transaction affects earnings. For further discussion regarding derivative financial instruments, refer to Note 6, Financial Instruments, to the accompanying consolidated financial statements.

**Recent Accounting Pronouncements** — The FASB ASC is the sole source of authoritative GAAP other than the SEC issued rules and regulations that apply only to SEC registrants. The FASB issues an ASU to communicate changes to the FASB codification. We assess and review the impact of all ASUs. ASUs not listed below were reviewed and determined to be either not applicable or are not expected to have a material impact on the consolidated financial statements.

#### Accounting Standards Adopted in 2018

**Modification Accounting for Share-Based Payment Awards** — Effective January 1, 2018, we adopted ASU No. 2017-09, Compensation – Stock Compensation (Topic 718) – Scope of Modification Accounting. The new standard clarifies when a change to the terms or conditions of a share-based payment award must be accounted for as a modification. Modification accounting is required if the fair value, vesting condition or the classification of the award is not the same immediately before and after a change to the terms and conditions of the award. We typically do not change either the terms or conditions of share-based payment awards once they are granted; therefore, the adoption of this new guidance had no impact on our consolidated financial statements.

**Restricted Cash — Statement of Cash Flows** — Effective January 1, 2018, we adopted ASU No. 2016-18, Statement of Cash Flows (Topic 230). The new standard requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash. Therefore, restricted cash should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on our consolidated Statement of Cash Flows. Accordingly, the statement of cash flows has been revised to include restricted cash (related to our capital and investment advisory services, as well as our property and casualty business unit) and cash equivalents associated with funds held to satisfy client obligations, as a component of cash, cash equivalents, restricted cash and cash equivalents. When restricted cash and cash equivalents are presented separately from cash and cash equivalents on the balance sheet, a reconciliation is required between the amounts presented on the statement of cash flows and the balance sheet, as well as a disclosure of information about the nature of the restrictions. The nature of the restrictions disclosure is included in the accompanying “Significant Accounting Policies.” The reconciliation of cash, cash equivalents and restricted cash as reported in the accompanying Consolidated Balance Sheets that sum to the total of the same such amount in the accompanying Consolidated Statements of Cash Flows is included below the accompanying Consolidated Statements of Cash Flows.

**Statement of Cash Flows** — Effective January 1, 2018, we adopted ASU No. 2016-15, Statement of Cash Flows (Topic 230) — Classification of Certain Cash Receipts and Cash Payments. The new standard provides guidance on eight specific cash flow issues. The application of this guidance did not have a material effect on the presentation of our consolidated Statement of Cash Flows.

**Revenue from Contracts with Customers** — Effective January 1, 2018, we adopted Topic 606 using the modified retrospective transition method. We recognized the cumulative effect of initially applying the new standard as an adjustment directly to the opening balance of “Retained earnings” at January 1, 2018. The comparative information has not been restated and continues to be reported under the legacy standard.

We evaluate our revenue contracts with customers based on the five-step model under Topic 606, pursuant to which we: (i) identify the contract with the customer; (ii) identify the performance obligation in the contract;

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(iii) determine the contract price; (iv) allocate the transaction price; and (v) recognize revenue when as each performance obligation is satisfied. If we determine that a contract with enforceable rights and obligations does not exist, revenues are deferred until all criteria for an enforceable contract are met.

Revenue recognition was consistent under both the legacy standard and Topic 606 for the majority of our revenue streams, with the exception of two business units within our Benefits and Insurance Services practice group.

- In our Property and Casualty business unit, commission revenue under agency billing arrangements (pursuant to which we bill the insured, collect the funds and remit the premium to the insurance carrier less our commissions) was previously recognized on the later of the effective date of the insurance policy or the date billed to the customer. We now recognize the commission revenue on the effective date of the insurance policy.
- Also in our Property and Casualty business unit, commission revenue under direct billing arrangements (pursuant to which the insurance carrier bills the insured directly and remits the commissions to us) was previously recognized when the data necessary from the carriers was available, whereas now we recognize the commission revenue on the effective date of the insurance policy.
- In our Retirement Plan Services business unit, under certain defined benefit administration arrangements we charge new clients an initial, non-refundable, set-up fee as part of a multi-year service agreement. Previously, these fees were recognized over the initial set up period, whereas now we defer the set-up fees and associated costs and recognize them over the life of the contract or the expected customer relationship, whichever is longer.

The cumulative effect of the changes made to our consolidated January 1, 2018 balance sheet was as follows (in thousands):

<u>Balance Sheet</u>	<u>Balance at December 31, 2017</u>	<u>Adjustments due to Topic 606</u>	<u>Balance at January 1, 2018</u>
<b>ASSETS</b>			
Accounts receivable, net .....	\$ 188,300	\$10,098	\$ 198,398
Other current assets .....	259,873	80	259,953
Other non-current assets .....	728,058	728	728,786
Total assets .....	<u>\$1,176,231</u>	<u>\$10,906</u>	<u>\$1,187,137</u>
<b>LIABILITIES</b>			
Accounts payable .....	51,375	6,281	57,656
Accrued personnel costs .....	45,264	595	45,859
Other current liabilities .....	237,607	113	237,720
Deferred income taxes, net .....	3,339	814	4,153
Other non-current liabilities .....	307,767	1,012	308,779
Total liabilities .....	<u>645,352</u>	<u>8,815</u>	<u>654,167</u>
<b>STOCKHOLDERS' EQUITY</b>			
Retained earnings .....	345,302	2,091	347,393
Other stockholders' equity .....	185,577	—	185,577
Total stockholders' equity .....	<u>530,879</u>	<u>2,091</u>	<u>532,970</u>
Total liabilities and stockholders' equity .....	<u>\$1,176,231</u>	<u>\$10,906</u>	<u>\$1,187,137</u>

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**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (continued)**

The following tables summarize the impact of adopting Topic 606 on our consolidated financial statements for the periods indicated below (in thousands):

<u>December 31, 2018</u> <u>Balance Sheet</u>	<u>As reported</u>	<u>Adjustments</u>	<u>Balances</u> <u>without</u> <u>adoption of</u> <u>Topic 606</u>
<b>ASSETS</b>			
Accounts receivable, net .....	\$ 207,287	\$(12,671)	\$ 194,616
Other current assets .....	216,251	(80)	216,171
Other non-current assets .....	759,493	(647)	758,846
Total assets .....	<u>\$1,183,031</u>	<u>\$(13,398)</u>	<u>\$1,169,633</u>
<b>LIABILITIES</b>			
Accounts payable .....	\$ 58,630	\$ (7,930)	\$ 50,700
Accrued personnel costs .....	63,953	(587)	63,366
Other current liabilities .....	198,731	(113)	198,618
Deferred income taxes, net .....	6,764	(1,035)	5,729
Other non-current liabilities .....	261,290	(897)	260,393
Total liabilities .....	589,368	(10,562)	578,806
<b>STOCKHOLDERS' EQUITY</b>			
Retained earnings .....	408,963	(2,836)	406,127
Other stockholders' equity .....	184,700	—	184,700
Total shareholders' equity .....	593,663	(2,836)	590,827
Total liabilities and stockholders' equity .....	<u>\$1,183,031</u>	<u>\$(13,398)</u>	<u>\$1,169,633</u>

<u>Year Ended December 31, 2018</u> <u>Income Statement</u>	<u>As reported</u>	<u>Adjustments</u>	<u>Balances</u> <u>without</u> <u>adoption of</u> <u>Topic 606</u>
Revenue .....	\$922,003	\$(1,039)	\$920,964
Operating expenses .....	790,283	(73)	790,210
Gross margin .....	131,720	(966)	130,754
Corporate general and administrative expenses .....	39,173	—	39,173
Operating income .....	92,547	(966)	91,581
Other (expense) income:			
Interest expense .....	(6,645)	—	(6,645)
Gain on sale of operations, net .....	1,025	—	1,025
Other expense, net .....	(7,087)	—	(7,087)
Total other expense, net .....	(12,707)	—	(12,707)
Income from continuing operations before income tax expense .....	79,840	(966)	78,874
Income tax expense .....	18,267	(221)	18,046
Income from continuing operations .....	61,573	(745)	60,828
Loss from discontinued operations, net of tax .....	(3)	—	(3)
Net income .....	<u>\$ 61,570</u>	<u>\$ (745)</u>	<u>\$ 60,825</u>

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Year Ended December 31, 2018 Cash Flow Statement	As reported	Adjustments	Balances without adoption of Topic 606
Cash flows from operating activities:			
Net income .....	\$ 61,570	\$ (745)	\$ 60,825
Adjustments to reconcile net income to net cash provided by operating activities: .....	38,713	—	38,713
Changes in assets and liabilities, net of acquisitions and divestitures:			
Accounts receivable, net .....	(10,668)	2,573	(8,095)
Other assets .....	(3,344)	(81)	(3,425)
Accounts payable .....	974	(1,649)	(675)
Accrued personnel costs .....	17,901	8	17,909
Other liabilities .....	(140)	(106)	(246)
Other .....	426	—	426
Operating cash flows provide by continuing operations ...	105,432	—	105,432
Operating cash flows used in discontinued operations ....	(184)	—	(184)
Net cash provided by operating activities .....	105,248	—	105,248
Net provided by investing activities .....	(47,576)	—	(47,576)
Net cash used in financing activities .....	(109,380)	—	(109,380)
Net increase in cash, cash equivalents and restricted cash ...	(51,708)	—	(51,708)
Cash, cash equivalents and restricted cash at beginning of year .....	182,262	—	182,262
Cash, cash equivalents and restricted cash at end of period .....	<u>\$ 130,554</u>	<u>\$ —</u>	<u>\$ 130,554</u>

**Accounting Standards Issued But Not Adopted at December 31, 2018**

**Internal-Use Software** — In August 2018, the FASB issued ASU 2018-15, Intangibles — Goodwill and Other — Internal-Use Software (Subtopic 350-40), which aligns the requirements for capitalizing implementation costs incurred in a service contract hosting arrangement with those of developing or obtaining internal-use software. This standard is effective for interim and annual reporting periods beginning after December 15, 2019, and early adoption is permitted. We do not expect this guidance to have a material impact on our consolidated financial position or results of operations.

**Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income** — In February 2018, the FASB issued ASU No. 2018-02, Income Statement — Reporting Comprehensive Income (Topic 220) which allows the reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Act. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods, with early adoption permitted. We do not expect this guidance to have a material impact on our consolidated financial position or results of operations.

**Derivatives and Hedging** — In August 2017, the FASB issued ASU No. 2017-12, Derivatives and Hedging (Topic 815) — Targeted Improvements to Accounting for Hedging Activities. The new standard improves and simplifies accounting rules for hedge accounting to better present the economic results of an entity's risk

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management activities in its financial statements and improves the disclosures of hedging arrangements. Additionally, it simplifies the hedge documentation and effectiveness assessment requirements. The updated guidance is effective for us beginning January 1, 2019. We do not expect this guidance to have a material impact on our consolidated financial position or results of operations.

**Leases** — In February 2016, the FASB issued the New Lease Standard. The new standard requires lessees to recognize a right-of-use asset and a lease liability for all leases (with the exception of short-term leases) on their balance sheet at the commencement date and recognize expenses on their income statement similar to the current guidance under ASC Topic 840, Leases. The New Lease Standard is effective for fiscal years and interim periods beginning after December 15, 2018. In addition, the FASB issued ASU No. 2018-11, Leases Targeted Improvements, which provides a package of practical expedients for entities to apply upon adoption.

We will adopt this standard effective January 1, 2019. We expect the New Lease Standard to have a material effect on our consolidated balance sheet, with no material impact on our results of operations, our liquidity or our debt covenant compliance under our current credit agreements. Refer to Note 11, Lease Commitments, to the accompanying consolidated financial statements for further information on our current lease arrangements, the amounts of which represent the future undiscounted commitments.

#### NOTE 2. REVENUE

In accordance with the new revenue recognition standard requirements, the following table disaggregates our revenue by source (in thousands):

	For the Year Ended December 31, 2018			
	Financial Services	Benefits & Insurance	National Practices	Consolidated
Accounting, tax, advisory and consulting . . . . .	\$600,926	\$ —	\$ —	\$600,926
Core Benefits and Insurance Services . . . . .	—	276,496	—	276,496
Non-core Benefits and Insurance Services . . . . .	—	11,941	—	11,941
Managed networking, hardware services . . . . .	—	—	24,404	24,404
National Practices consulting . . . . .	—	—	8,236	8,236
<b>Total revenue . . . . .</b>	<b>\$600,926</b>	<b>\$288,437</b>	<b>\$32,640</b>	<b>\$922,003</b>

#### Financial Services

Revenue primarily consists of professional service fees derived from traditional accounting services, tax return preparation, administrative services, financial and risk advisory, consulting and valuation services. Clients are billed for these services based upon a fixed-fee, an hourly rate, or an outcome-based fee. Time related to the performance of all services is maintained in a time and billing system.

Revenue for fixed-fee arrangements is recognized over time with the performance obligation measured in hours worked and anticipated realization. Anticipated realization is defined as the fixed fee divided by the product of the hours anticipated to complete a performance obligation and the standard billing rate. Anticipated realization rates are applied to hours charged to a contract when recognizing revenue. At the end of each reporting period, we evaluate the work performed to date to ensure that the amount of revenue recognized in each reporting period for the client arrangement is equal to the performance obligations met.

Time and expense arrangement revenue is recognized over time with progress measured towards completion with value being transferred through our hourly fee arrangement at expected net realizable rates per hour, plus agreed-

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upon out-of-pocket expenses. The cumulative impact on any subsequent revision in the estimated realizable value of unbilled fees for a particular client project is reflected in the period in which the change becomes known.

We applied the guidance of Topic 606 in determining the appropriate accounting for outcome-based arrangements. Prior to recognizing revenue, we estimate the transaction price, including variable consideration that is subject to a constraint based on risks specific to the arrangement. We evaluate the estimate in each reporting period and recognize revenue to the extent it is probable that a significant reversal of revenue will not occur. Revenue is recognized when the constraint is lifted at a point in time when the value is determined and verified by a third party.

#### Benefits and Insurance Services

Core Benefits and Insurance Services consists of group health benefits consulting, property and casualty, retirement plan services and payroll processing services. Revenue consists primarily of fee income for administering health and retirement plans and brokerage commissions. Revenue also includes investment income related to client payroll funds that are held in CBIZ accounts, as is industry practice. Under the new revenue recognition standard, the cost to obtain a contract must be capitalized unless the contract period is one year or less. We pay commissions monthly and require the recipient of the commission to be employed by us at the time of the payment. Failure to remain employed at the date the commission is payable results in the forfeiture of commissions that would otherwise be due. Therefore, we have determined that the requirement of continued employment is substantive and accordingly, do not consider the commissions to be incremental costs of obtaining the customer contract and consequently a contract acquisition cost is not recognized for those commissions.

Revenue related to group health benefits consulting consists of (i) commissions, (ii) fee income which can be fixed or variable based on a price per participant and (iii) contingent revenue.

- Commission revenue and fee income are recognized over the contract period as these services are provided to clients continuously throughout the term of the arrangement. Our customers benefit from each month of service on its own and although volume and the number of participants may differ month to month, the obligation to perform substantially remains the same.
- Contingent revenue arrangements are related to carrier-based performance targets. Due to the uncertainty of the outcome and the probability that a change in estimate would result in a significant reversal of revenue, we have applied a constraint on recording contingent revenue. Revenue is recognized when the constraint has been lifted which is the earlier of written notification that the target has been achieved or cash collection. Contingent revenue is not a significant revenue stream to our consolidated financial position or results of operations.

Revenue related to property and casualty consists of (i) commissions and (ii) contingent revenue.

- Commissions relating to agency billing arrangements (pursuant to which we bill the insured, collect the funds and forward the premium to the insurance carrier less our commission) and direct billing arrangements (pursuant to which the insurance carrier bills the insured directly and forwards the commission to us) are both recognized on the effective date of the policy. Commission revenue is reported net of reserves for estimated policy cancellations and terminations. The cancellation and termination reserve is based upon estimates and assumptions using historical cancellation and termination experience and other current factors to project future experience.
- Contingent revenue arrangements related to carrier-based performance targets include claim loss experience and other factors. Due to the uncertainty of the outcome and the probability that a change in

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estimate would result in a significant reversal of revenue, we have applied a constraint on recording contingent revenue. Revenue is recognized when the constraint has been lifted which is the earlier of written notification that the target has been achieved or cash collection. Contingent revenue is not a significant revenue stream to our consolidated financial position or results of operations.

Revenue related to retirement plan services consist of advisory, third party administration and actuarial services.

- Advisory revenue is based on the value of assets under management, as provided by a third party, multiplied by an agreed upon rate. Advisory services revenue is calculated monthly or quarterly based on the estimated value of assets under management, as it is earned over the duration of the reporting period and relates to performance obligations satisfied during that period. The variability related to the estimated asset values used to recognize revenue during the reporting period is resolved and the amount of related revenue recognized is adjusted when the actual value of assets under management is known.
- Third party administration revenue is recognized over the contract period as these services are provided to clients continuously throughout the term of the arrangement. Our clients benefit from each month of service on its own, and although the volume of tasks may differ month to month, the obligation to perform substantially remains the same.
- Actuarial revenue is recognized over the contract period with performance measured in hours in relation to the expected total hours. Under certain defined benefit plan administration arrangements, we charge new clients an initial, non-refundable, set-up fee as part of a multi-year service agreement. Revenue and costs related to the set-up fees are deferred and recognized over the life of the contract or the expected customer relationship, whichever is longer.

Revenue related to payroll processing consists of a (i) fixed fee or (ii) variable fee based on a price per employee or check processed. Revenue is recognized when the actual payroll processing occurs. Our customers benefit from each month of service on its own and although volume and the variability may differ month to month, the obligation to perform substantially remains the same.

Non-core Benefits and Insurance Services consists of transactional businesses that tend to fluctuate. These include life insurance, wholesale agency benefits and talent and compensation services.

#### **National Practices**

Managed networking, hardware services revenue consists of installation, maintenance and repair of computer hardware. These services are charged to a single customer based on cost plus an agreed-upon markup percentage, which has existed since 1999.

National Practices consulting revenue is based upon a fixed fee, an hourly rate, or outcome-based. Revenue for fixed fee and time and expense arrangements is recognized over the performance period based upon actual hours incurred, while revenue for outcome-based arrangements is recognized similar to the outcome-based arrangements in the Financial Services practice group.

**Transaction Price Allocated to Future Obligations** — The new revenue recognition standard requires the disclosure of the aggregate amount of transaction price allocated to performance obligations that have not yet been satisfied as of the reporting date. The guidance provides certain practical expedients that limit this requirement, including performance obligations that are part of a contract that is one year or less. Since the majority of our contracts are one year or less, we have applied this practical expedient related to quantifying remaining performance obligations. In regards to contracts with terms in excess of one year, certain contract

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periods related to our government healthcare consulting, group health and benefits consulting, and property and casualty insurance businesses have an original specified contract duration in excess of one year, however, the agreements provide CBIZ and the client with the right to cancel or terminate the contract with no substantial penalty. We have applied the provisions of Topic 606 and the FASB Transition Resource Group memo number 10-14, and note that the definition of contract duration does not extend beyond the goods and services already transferred for contracts that provide both the Company and the client with the right to cancel or terminate the contract with no substantial penalty.

#### NOTE 3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net balances at December 31, 2018 and 2017 were as follows (in thousands):

	<u>2018</u>	<u>2017</u>
Trade accounts receivable .....	\$159,992	\$139,730
Unbilled revenue, at net realizable value .....	60,684	62,397
Total accounts receivable .....	220,676	202,127
Allowance for doubtful accounts .....	(13,389)	(13,827)
Accounts receivable, net .....	<u>\$207,287</u>	<u>\$188,300</u>

Changes in the allowance for doubtful accounts on accounts receivable are as follows (in thousands):

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Balance at beginning of period .....	\$(13,827)	\$(13,508)	\$(12,659)
Provision for losses .....	(3,776)	(5,529)	(4,154)
Charge-offs, net of recoveries .....	4,214	5,210	3,305
Balance at end of period .....	<u>\$(13,389)</u>	<u>\$(13,827)</u>	<u>\$(13,508)</u>

#### NOTE 4. PROPERTY AND EQUIPMENT, NET

Property and equipment, net at December 31, 2018 and 2017 consisted of the following (in thousands):

	<u>2018</u>	<u>2017</u>
Buildings and leasehold improvements .....	\$ 28,456	\$ 26,289
Furniture and fixtures .....	27,690	25,835
Capitalized software .....	37,281	36,639
Equipment .....	17,875	13,615
Total property and equipment .....	111,302	102,378
Accumulated depreciation and amortization .....	(77,097)	(76,297)
Property and equipment, net .....	<u>\$ 34,205</u>	<u>\$ 26,081</u>

Depreciation expense for property and equipment was \$6.1 million, \$5.3 million and \$5.4 million in 2018, 2017 and 2016, respectively.