

# Revenue Recognition Case Study

## HOSPITALITY INDUSTRY:

### SCENARIO:

A local restaurant offers a loyalty program to customers. Customers earn 1 point for every \$2 spent at the restaurant. When a customer has accumulated 100 points they can earn \$5 off their next purchase.

Through one month of the year the restaurant has had \$500,000 in sales, which correlates to 250,000 outstanding loyalty points.

Based on history of the program, the restaurant expects 63% of loyalty points to be redeemed.

### STEP ONE - IDENTIFY THE CONTRACT WITH A CUSTOMER

The restaurant will provide meal and loyalty program to customer.

### STEP TWO - IDENTIFY PERFORMANCE OBLIGATIONS IN THE CONTRACT

What is the total number of Performance Obligations?

Two – meal and loyalty program

### STEP THREE - DETERMINE THE TRANSACTION PRICE

In total for the quarter the transaction price is \$500,000.

### STEP FOUR - ALLOCATION OF TRANSACTION PRICE

The transaction price should be allocated to the performance obligations based on standalone price of each performance obligation.

	CONTRACT	STANDALONE	ALLOCATION
Sales	\$500,000	\$500,000	\$492,247
Loyalty Program	-	\$7,875	\$7,753
	<u>\$500,000</u>	<u>\$507,875</u>	<u>\$500,000</u>

The stand alone selling price of the loyalty program is calculated as follows:

Total loyalty points value $((250,000/100)*5)$	\$12,500
Likelihood of use	<u>63%</u>
Loyalty program standalone price	\$7,875

## STEP FIVE - RECOGNIZE REVENUE

Below are the required journal entries to recognize the above transactions:

RECORD MONTHLY SALES						
Cash			\$500,000			
	Contract Liability		-			\$7,753
	Revenue					\$492,247
End of Month 1 - 111,000 loyalty points had been redeemed						
Contract Liability			\$5,464			
	Revenue				\$5,464	
		Redeemed	111,000			
	Anticipated Redeemed		157,500	70.5%	\$5,463.94	% times allocation
Balance of contract liability at the end of month 1.						\$2,289
End of Month 2 - 44,610 additional loyalty points had been redeemed						
Contract Liability			\$2,196			
	Revenue				\$2,196	
		Redeemed	155,610			
	Anticipated Redeemed		157,500	98.8%	\$7,660	% times allocation
Balance of contract liability at the end of month 2						93

If at the end of month 2 we determine our estimated usage was too low, the standard requires breakage to be accounted for by way of a cumulative catch up adjustment to revenue. A change in price is not the same as a change in estimate (breakage), therefore the allocation of price is not recalculated.

During Month 2 - 44,610 additional loyalty points had been redeemed and the breakage is now expected to be at 67%						
Contract Liability			\$1,739			
	Revenue					\$1,739
		Redeemed	155,610			
	Anticipated Redeemed		167,500	92.9%	\$7,203	% * allocation
Balance of contract liability at the end of month 2						550

## DO YOU UNDERSTAND THE IMPACT OF THE NEW ACCOUNTING STANDARDS ON YOUR HOSPITALITY COMPANY?

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For additional details on the new revenue recognition accounting rules or to learn more about how we can help, please contact a Smith Schafer professional at [info@smithschafer.com](mailto:info@smithschafer.com).