

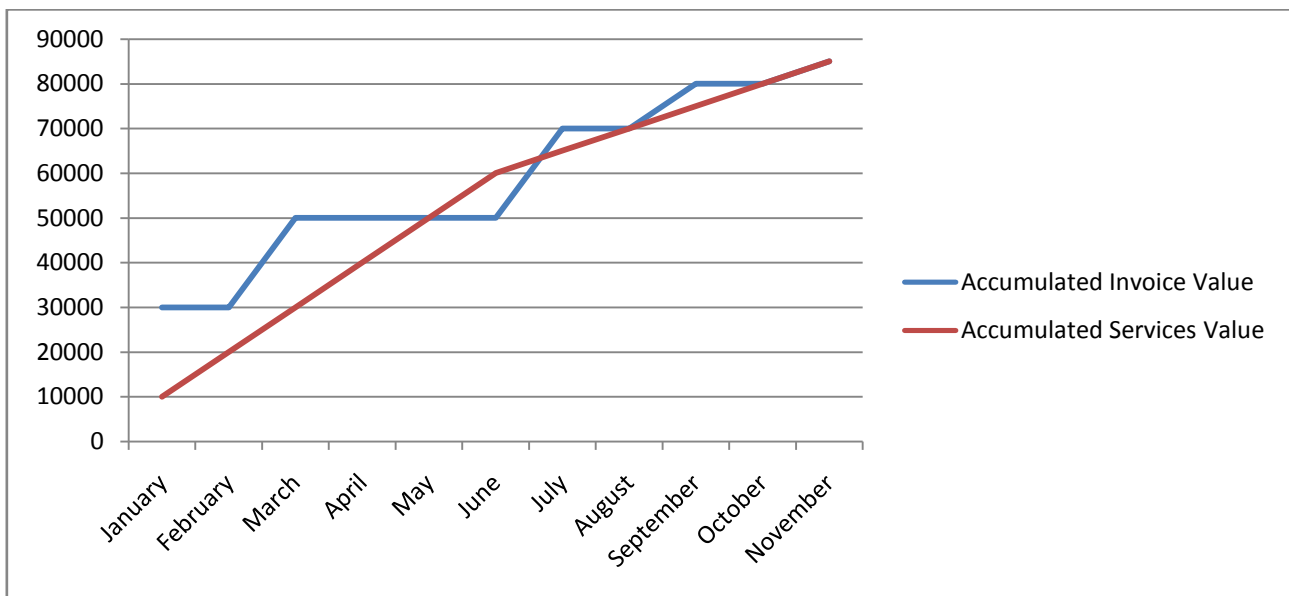
Briefing: Revenue Recognition

Many service organisations provide services on a fixed-price fixed-scope basis and invoice to an agreed timetable that might not reflect the value of completed work. In today's economic climate, investors, customers and partners are demanding responsible revenue recognition. The post dot-com shakeout, together with several high-profile stories has helped to move this accounting issue up to the top of the boardroom agenda. In the past stakeholders may have been happy to trust that a competent CFO will ensure that revenue is recognised in an appropriate manner, it is becoming increasingly important to have explicit policies in place and to make them clear.

In this briefing we will look at an example of a services company with a long-term project and explore the accounting implications of revenue recognition and how time@work can help to manage this. In this example invoices are raised to a planned timetable:

Month	Invoice Value
January	30000
March	20000
July	20000
September	10000
November	5000
December	10000

However in practice there will often be a discrepancy between the invoice timetable and the services carried out.



When the value of invoices raised does not reflect the value of the services provided (at the rates implied by the fixed price contract), it is imprudent to recognise full invoice value as revenue. In this example the amount of revenue to recognise can be properly expressed as follows:

$$\text{Revenue To Recognise} = \text{Full Project Revenue} * (\text{Completed Services/Planned Services})$$

Note that recognised revenue should never exceed accumulated invoice value (on the assumption that Work in Progress is accounted for separately).

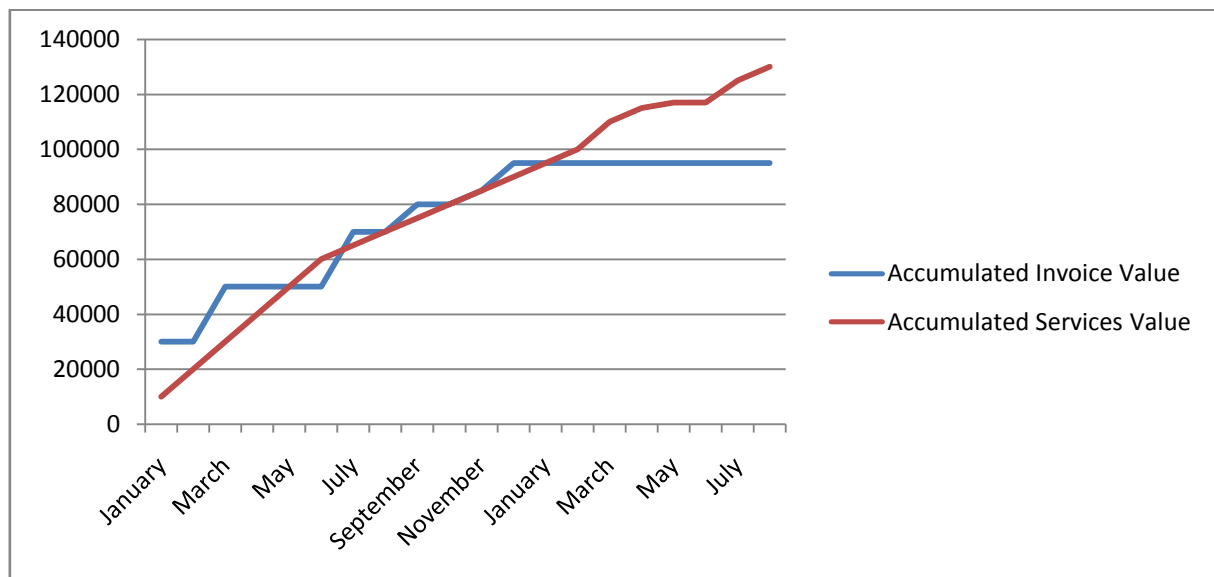
In this example the revenue to recognise is as follows:

Month	Invoiced Value	Accumulated Invoice Value	Accumulated Services Value	Revenue To Recognise
January	30000	30000	10000	10555
February		30000	20000	21111
March	20000	50000	30000	31666
April		50000	40000	42222
May		50000	50000	50000
June		50000	60000	50000
July	20000	70000	65000	68611
August		70000	70000	70000
September	10000	80000	75000	79166
October		80000	80000	80000
November	5000	85000	85000	85000
December	10000	95000	90000	95000

Here a planned services value of 90,000 was invoiced at 95,000, reflecting a contingency of 5,000 built into the plan in advance. The full value of services provided has been “realised”.

Unfortunately projects often overrun their planned timescales and the additional services cannot always be invoiced. When this happens the risks associated with improper revenue recognition are more serious.

In this case none of the service value provided in the second year of the project can be “realised”, though real costs in the second year continue to accumulate. When this situation occurs an accurate estimate of the efforts required to complete a project must be kept up to date and revenue recognised in proportion to the full effort required for completion.



The following table shows how revenue might be recognised in this case.

Month	Invoiced Value	Accumulated Invoice Value	Accumulated Services Value	Estimated Value To Completion	Revenue To Recognise
January	30000	30000	10000	90000	10556
February		30000	20000	90000	21111
March	20000	50000	30000	90000	31667
April		50000	40000	100000	38000
May		50000	50000	100000	47500
June		50000	60000	100000	57000
July	20000	70000	65000	100000	61750
August		70000	70000	105000	63333
September	10000	80000	75000	105000	67857
October		80000	80000	105000	72381
November	5000	85000	85000	105000	76905
December	10000	95000	90000	110000	77727
January		95000	95000	115000	78478
February		95000	100000	115000	82609
March		95000	110000	120000	87083
April		95000	115000	125000	87400
May		95000	117000	125000	88920
June		95000	117000	125000	88920
July		95000	125000	130000	91346
August		95000	130000	130000	95000

Using time@work to enable the correct calculation of Revenue Recognition

Using time@work it is possible to capture the following:

1. **Actual time spent on projects, tasks and activities:** These values derive from Employee's timesheets posted to the Project Ledger.
2. **Actual invoices for projects, tasks and activities:** Project invoices can be created as ad-hoc invoices or from work in progress (optionally from planned invoices stored in the planned invoice ledger). Invoices are posted to the Project Ledger.
3. **Outstanding planned invoices for projects, tasks and activities:** These are the residual (un-invoiced) invoices in the Planned Invoice Ledger.
4. **Up to date project plans:** A project plan showing latest estimates for service days or value can be maintained in a Project Ledger (or imported from an MS-Project file).



A

C



B



D

Invoiced Value To Date	Outstanding Planned Invoice Value	Total Invoice Value	Time To Date	Total Estimated Time	Revenue To Recognise
A	B	(A+B)	C	D	(A+B) * (C/D)

It is then a simple matter to calculate and report on recognisable revenue using time@work Inquiry Profiles.