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Balance sheet

# Revenue Recognition for Construction Contracts

By Angie Bursby, CPA

In May of 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09 titled Revenue from Contracts with Customers. Although this new standard will not fundamentally change how most construction contractors have been recording revenue, it will require more disclosures with the financial statements that will provide information about the construction contracts and the judgements made in accounting for those contracts.

ASU 2014-09 is effective for nonpublic companies beginning on or after December 15, 2018; however, early application can be used as soon as December 15, 2016. The core principle underlying this new standard is that an entity will recognize revenue as it meets a performance obligation (a promise in a contract with a customer to transfer goods or services) in the contract. There is a 5-step model that will be used to implement the new standard. First, a contract with a customer will be identified. Once the contract has been established and agreed upon, the performance obligations included in the contract will be identified. Construction contracts may contain one or more performance obligations. The third step will be to determine the transaction price, which will be the amount the contractor is entitled to for the exchange of goods and services. The fourth step will be to allocate the transaction price to the performance obligations in the contract. Finally, the contractor will then recognize revenue as they satisfy each performance obligation. For construction contracts, the company will be able to select an input or output method (such as cost-to-cost) to measure the progress toward satisfaction of the performance obligation. For the construction industry, transfer of control generally occurs over a period of time; and, therefore application of the new standard to construction contracts could result in a similar revenue recognition pattern to what is used currently. However, in order for contractors to recognize the revenue over a period of time (similar to percentage-of-completion), one or more of the following criteria must be met: the customer simultaneously receives and consumes the benefits provided by the contractor's performance as they are performed; the contractor's performance creates or enhances an asset that the customer controls; and the contractor's performance does not create an asset with an alternative use to the contractor as well as providing the contractor with an enforceable right to payment for the performance completed to date. If none of these three criteria are met, then revenue will need to be recognized at a certain point in time rather than over time, typically when the contract is finished.


The purpose of the new standard is to increase financial statement comparability across companies and industries so that revenue recognition is more standardized and more simplified. While it may not appear to simplify the process in the beginning, once the new standard is implemented, it should be fairly easy to identify those key performance obligations going forward and recognize the revenue as they are satisfied. If you have any questions regarding the application of this new standard to your company, please contact us and we will be glad to help with the implementation process.