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March 10, 2012

Acct 305

### Revenue Recognition: Identifying The Contract with A Customer

Applying revenue recognition is the process of a customer giving a company or seller money and in exchange receiving a type of good or service. The amount of revenue received and the distribution of goods are based on the seller's discretion. How Revenue Recognition is proposed is with a five-step process. These five- steps include: identifying a contract to a customer, identifying performance, determining the transaction price, allocating the transaction price, and recognizing the revenue. Step one of the process is what is crucial in revenue recognition because there must be a mutual understanding between the seller and customer before any contracts can be created. Without a clear step 1 the rest of the revenue recognition process would be meaningless.

A contract is made between the customer and seller to identify the agreement to the customer in the first of the five-step process. Without a clear understanding of what is expected from both parties, future issues can arise. A contract is known as an agreement between at least two parties to create the obligations of what is being arranged. Although a written contract is usually more convenient and secure the agreement can be either written or oral. The decision of what type of contract is under the discretion of the parties. To make sure a contract is strong the contract must have enforceable obligations so that if the rights of the contract are ever broken for any unjust reason there can be a penalty. Without

strong fines or penalties, contracts can be broken at any time, which than results in loss of revenue for the seller. The seller of the good decides the penalties of a broken contract.

In order for a contract to be considered legal it must have been approved by both parties before any transactions take place. For a company it is crucial for them to identify any payment terms that will be taken place before the contract is official. Without payment terms set before could result in a loss of revenue for the company.

The second part of identifying a contract to a seller is determining if a combined contract needs to be made when a seller and customer are having two transactions one after the other. Another main trait in identifying if a contract should be combined is whether the goods or services being sold are performance combined. For example if a customer wants to buy a MacBook and a charger for the laptop the transactions can be sold together because they are from one company and are used together. A contract may not be combined if the goods or service has separate performance duties or different companies are selling one customer two different goods.

Having clear contracts for any goods being sold to customers gives a seller an upper hand over any other company who may sell the same products. Companies like Nordstrom have strong customer support and high profits because of their great return policies regarding any good they sell. Nordstrom's makes it clear in any transaction they occurs that if a customer is ever unhappy with any good they may have purchased they can always return for the purchase price. This type of loyalty has kept their customers devoted and returning for years.

Not only is having a clear contract beneficial financially for a seller and customer, but it is also convenient. If anything ever goes wrong between the transactions there can always be written documentation.