

# Written project base on case study

Education



From the case we discuss, LabCo's accounting policy for recognizes revenue from construction contract is reasonable. According to ASC605-35-25-61, an entity... shall use the completed-contract... for which reasonably dependable estimates cannot be made or for which inherent hazards make estimates doubtful. LabCo Company uses a normal standard for its accounting policy which is using Percentage of completion method base on how it determine the profit (cost-to-cost method); but in contract with Halibut, LabCo experiences unexpected difficulties includes: revising design, outsourcing engineering, price of material rising unforeseeably.

These are the factors that make cost estimation harder. Percentage of Completion method is appropriate under ASC605-35-25-57, criteria B, The buyer can be expected to satisfy all obligations under the contract and C, The contractor can be expected to perform all contractual obligations.

Completion of contract method is used according to ASC605-32-25-90, When lack of dependable estimates...inherent hazards relate to contract conditions or external factors that raise questions about contract estimates and about the ability of either the contractor or the customer to perform all obligations under the contract.

Percentage of completion method is inappropriate for this contract, not only because it's difficult to estimate the cost, but also the product fails to fulfill the buyer's need. In this case, choosing completion of contract is better decision; based on previous experience, LabCo underestimate the cost and ability of complete the contract is the main reason forces them to change the policy.

Change in method of accounting from the percentage-of-completion to the completed-contract is considering change in accounting principle. In ASC250-10-45-2, it states clearly about company can use alternative accounting principle to better interpret the current financial issues. According to ASC250-10-45-1, a presumption exists that an accounting principle once adopted shall...consistent use of the same accounting principle from one accounting period to another...and with a, b criteria.

Once a new accounting principle is adopted, entity should consistently practice. Base on ASC250-10-45-5, entity should use retrospective approach apply for the new accounting principle. There are three basic requirements to do: A. Back to prior accounting period, the change of cumulative effect must be showed once apply the new principle. B. adjustment of the balance of retained earning must be made. C. Each individual financial statement from prior period shall apply the new principle.

In LabCo's case, once it changes the revenue recognition principle, the prior year's revenue will become less in completion of contract method. Retain Earning account must be higher when using percentage of completion method. Therefore, retained earnings account needs to be adjusted. For current year, adjustment shall be made to beginning balance of retained earnings. Base on ASC250-10-45-8, Retrospective application shall include only the direct effects of a change in accounting principle, including any related income tax effects.

Using retrospective approach shall contain direct effects, in this case would be income tax from prior period which should be less than the entity actual

paid. Disclosure, ASC250-10-50-2 An entity that issues interim financial statements shall provide the required disclosures in the financial statements of both the interim period of the change and the annual period of the change. When reporting a change in Principle, explanation of why use new principle should be included.

### **Work Cited**

Kieso, D. E., T. D. Warfield, and J. J. Weygandt. Intermediate accounting. 14th. Hoboken: John Wiley& Sons, Inc. , 2012. Print. <https://asc.fasb.org/advancedsearchresults>