

# Zynga's revenue recognition dilemma

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Zynga's Revenue Recognition Dilemma Zynga has been the focus of a highly disputed topic on bookings and revenues as of late. Unfortunately for the online gaming company, many accountants and financial analysts are not in Zynga's favor on the way that the company has been recognizing revenues. To put the company in perspective, there are 26 million digital farmers via the vastly rampant FarmVille application run by Zynga.

In the popular game, Facebook users build farms to produce crops and create the kind of productivity that they desire. This creates the need for virtual, heavy equipment, such as tractors, seeders and harvesters, all which can be bought with FarmVille Currency. Zynga makes money by allowing users to hurry the process by converting real dollars from their credit cards into the virtual currency necessary to get the equipment they need to get the job done. Like FarmVille, Zynga has users across a variety of applications such as CityVille, Words with Friends, and Mafia Wars, all of which using the same models.

This type of unique revenue however provokes a unique question; that is, how is Zynga supposed to report revenues from these products that they've offered? According to the company's 10-k report, it's policies on reporting states that: \* " For the sale of consumable virtual goods, we recognize revenue as the goods are consumed" \* " We recognize revenue from the sale of durable virtual goods ratably over the estimated average playing period of paying players for the applicable game, which represents our best estimate of the average life of our durable virtual goods" And perhaps the

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most important: “ If we do not have the ability to differentiate revenue attributable to durable virtual goods from consumable virtual goods for a specific game, we recognize revenue from the sale of durable and consumable virtual goods for that game ratably over the estimated average period that paying players typically play our games” This type of financial reporting is simply too confusing and leaves the door open for too much alteration within the reports. Also, this type of unpredictable reporting technique allows the company to skew bottom-line profits and maneuver their earnings to reflect an untrue valuation of the company's worth.

These types of manipulations are especially alarming to users of the financials who are looking to invest in a company that appears to be growing, when in reality it is altering production numbers with every consecutive quarter. In regards to the revenue recognition dispute, the way their accountants estimate average periods that paying players actually play the Zynga games must be validated. In a recent article by Bloomberg's Cory Johnson, he notes that Zynga has made changes to these estimates five of the last six quarters. These changes made drastically effect the net profits that Zynga is reporting to the public.

By taking the estimate and distorting it, they are able to report profits when indeed there are none. It is curious that the auditor assigned to Zynga, Ernst & Young, has allowed this method of accounting to be implemented when clearly it is affecting the bottom line. It is also curious that E&Y is also the auditor for the Zynga's distributor, Facebook whose Zynga profits have accounted for roughly 12% of its revenue. This “ independence” (or lack there of) calls into question the true authenticity behind these reporting

standards and what they mean to the accounting profession as well as financial statement users world-wide.

At any rate, this is a topic that needs to be brought to light, discussed and ruled upon. Zynga cannot merely go on reporting as they wish to provoke the appearance of a success while the true profits and losses go unnoticed.

<http://blogs.smeal.psu.edu/grumpyoldaccountants/archives/746#more-746>

[http://articles.businessinsider.com/2011-10-12/research/30269486\\_1\\_zynga-virtual-goods-bookings](http://articles.businessinsider.com/2011-10-12/research/30269486_1_zynga-virtual-goods-bookings)

<http://www.forbes.com/sites/francinemckenna/2012/04/23/how-zynga-facebook-and-groupons-go-to-auditor-rewrites-accounting-rules/>

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