

ACCOUNTANCY 422
LONG TERM CONSTRUCTION CONTRACT
SUPPLEMENTAL PROBLEM SOLUTION

a. Calculation of revenue.

$$\text{Year 1 Revenue} = (\$10,500,000 \div \$42,000,000 * \$50,000,000) - \$0 = \$12,500,000$$

$$\begin{aligned} \text{Year 2 Revenue} &= (\$33,000,000 \div \$44,000,000 * \$50,000,000) - \$12,500,000 \\ &= \$25,000,000 \end{aligned}$$

$$\begin{aligned} \text{Year 3 Revenue} &= (\$44,000,000 \div \$44,000,000 * 50,000,000) - \$37,500,000 \\ &= \$12,500,000 \end{aligned}$$

b. Calculation of account balances:

Billings recorded in Year 1	\$10,000,000
Revenues recognized in Year 1	<u>– \$12,500,000</u>
Costs and profits in excess of billings, Year 1	<u>\$ 2,500,000</u>

Billings recorded in Year 2	\$20,000,000
Revenue recognized in Year 2	<u>– 25,000,000</u>
Costs and profits in excess of billings for Year 2	5,000,000
Beginning balance of Costs and profits in excess of billings	<u>2,500,000</u>
Ending Year 2 balance of Costs and Profits in excess of billings	<u>\$ 7,500,000</u>

c. Journal entries for year 2:

Construction expenses	\$22,500,000	
Cash		\$22,500,000
To record costs as incurred		

Accounts receivable	\$20,000,000	
Construction revenue		\$20,000,000
To record billings to customers		

Cash	\$20,000,000	
Accounts receivable		\$20,000,000
To record collections from customers.		

Costs and profits in excess of billings	\$5,000,000	
Construction revenue		\$5,000,000
To adjust revenue account.		

d. Journal entries to adjust revenue for year 3:

Revenue recorded		\$20,000,000
Revenue to be recognized		<u>12,500,000</u>
Adjustment to revenue and to Cost and Profits in Excess of Billings		<u>\$ 7,500,000</u>
Construction revenue	\$7,500,000	
Costs and Profits in Excess of Billings		\$7,500,000
To adjust revenue under the percentage of completion method		