

Case 18-3c
Nailed It! Construction

Nailed It! Construction (Nailed It! or the “Company”), an SEC registrant, is a construction company that manufactures commercial and residential buildings. On March 1, 20X1, the Company entered into an agreement with a customer, Village Apartments, to construct a residential apartment building for a fixed price of \$1.5 million. The Company estimates that it will incur costs of \$1 million to complete construction of the apartment building. The apartment building will only transfer to Village Apartments once the construction of the entire building is complete. In addition, Village Apartments has various design requirements that would require Nailed It! to incur significant costs to rework the building prior to selling it to a customer other than Village Apartments.

To construct the apartment building, Nailed It! acquires standard materials that it regularly uses in construction contracts for both residential and commercial buildings. These materials are used to manufacture generic component parts for inclusion in Village Apartments’ residential buildings. These standard materials remain interchangeable with other items until they are deployed in a Village Apartments building. The Company has made the following purchases and incurred the following costs throughout the construction progress:

- As of June 30, 20X1, in total, Nailed It! has purchased \$75,000 of component parts. As of June 30, 20X1, \$25,000 of component parts remain in inventory and \$50,000 have been integrated into the project. Further, Nailed It! has incurred \$12,500 of direct costs to integrate the component parts into the Village Apartments construction project during the three months ended June 30, 20X1.
- During the three months ended September 30, 20X1, Nailed It! purchased an additional \$500,000 of component parts (\$575,000 in total). Of the \$575,000 of component parts, \$325,000 remain in inventory and \$200,000 have been integrated into the project during the three months ended September 30, 20X1 (\$250,000 have been integrated into the project during the six months ended September 30, 20X1). During the three months ended September 30, 20X1, Nailed It! incurred an additional \$50,000 of direct costs to integrate the component parts into the Village Apartments construction project.
- As of September 30, 20X1, Nailed It! determined that the project was over budget and revised its cost estimate from \$1 million to \$1.25 million.
- As of December 31, 20X1, the construction project was completed. During the three months ended December 31, 20X1, Nailed It! purchased an additional \$425,000 of generic component parts (\$1 million in total). Of the \$1 million component parts, \$0 remain in inventory and \$750,000 were integrated into the project during the three months ended December 31, 20X1 (all \$1,000,000 have been integrated into the project during the year ended December 31, 20X1). Nailed It! has incurred \$187,500 of direct costs to integrate the component parts into the Village Apartments construction project during the three months ended December 31, 20X1.

If Village Apartments cancels the contract, Nailed It! will be entitled to reimbursement

for costs incurred for work completed to date plus a margin of 20 percent, which is considered to be a reasonable margin. Nailed It! will not be reimbursed for any materials that have been purchased for use in the contract but have not yet been used and are still controlled by Nailed It!

Required:

1. Does the performance obligation meet any of the criteria for recognition of revenue over time?
2. How should the entity recognize revenue for the satisfaction of its performance obligation? What amount of revenue should be recognized for the following periods:
 - 2a. The three months ended June 30, 20X1?
 - 2b. The three months ended September 30, 20X1?
 - 2c. The three months ended December 31, 20X1?