Exercise 1--Revenue Recognition

1. I buy a BOS-LAX ticket from Delta on 23 March 2015, paying in cash the fare of $1,000. I complete my travel on 31 December 2015. Delta credits my Sky Miles account with 7,500 miles. Can Delta recognize the entire $1,000 as revenue in 2015? Why or why not?

2. Electric City is a large retailer of televisions, stereos and appliances. They also sell three-year extended warranty contracts. Should Electric City recognize all of the revenue from extended warranties in the year it sells the televisions? Would your answer change if it were the case that Electric City prices the television and extended warranty as a “bundle”, with a very low profit margin on the television and a very high margin on the extended warranty?

3. Houghton Mifflin publishes books and magazines, distributing them through bookstores like Barnes and Noble. In its sales arrangement with Houghton Mifflin, Barnes and Noble is allowed to return all of the unsold books and magazines to Houghton Mifflin for a full refund. Suppose Houghton Mifflin sells 10,000 copies of a literary novel to Barnes and Noble on 15 June at a price of $12 per copy. Houghton Mifflin keeps extensive data on previous transactions with booksellers. On average, Barnes and Noble returns 17% of the copies literary novels. Can Houghton Mifflin recognize any revenue on 15 June? If not, then, when can it recognize revenue?