

ASC 606 REVENUE RECOGNITION MEMORANDUM

TO: Chief Accounting Officer **FROM:** Technical Accounting Team - AI **DATE:** August 21, 2025 **RE:** Contract Analysis - ASC 606 Revenue Recognition Analysis

BACKGROUND

We have reviewed the contract documents provided by Customer to determine the appropriate revenue recognition treatment under ASC 606. This memorandum presents our analysis following the five-step ASC 606 methodology and provides recommendations for implementation.

ASC 606 ANALYSIS

Identify the Contract

Analysis:

To determine if a valid contract exists under ASC 606-10-25-1, we must evaluate several criteria:

- Approval and Commitment (ASC 606-10-25-1(a)):** The contract is entered into by InnovateTech Solutions Inc. and Global Dynamics Corp. as of October 26, 2023, under the terms of a Master Services Agreement dated January 15, 2022. This indicates that both parties have approved the contract and are committed to performing their respective obligations. The presence of a signed Statement of Work (SOW) further supports this conclusion.
- Identification of Rights (ASC 606-10-25-1(b)):** The contract clearly identifies each party's rights regarding the goods and services to be transferred. InnovateTech is obligated to provide the Logi-AI Suite SaaS License, 200 OptiScan-7 scanners, and professional services for integration and training. The customer, Global Dynamics, is entitled to these deliverables as specified in the SOW.
- Payment Terms (ASC 606-10-25-1(c)):** The payment terms are explicitly outlined in the contract. The Logi-AI Suite SaaS License is priced at 240,000 per year, payable annually. The hardware and professional services are subject to one-time fees of 50,000 and 75,000, respectively, both due Net 30 from the Effective Date. Additionally, a performance bonus of 30,000 is contingent upon achieving a 15% reduction in shipping costs.

4. **Commercial Substance (ASC 606-10-25-1(d)):** The contract has commercial substance because it is expected to change the risk, timing, or amount of InnovateTech's future cash flows. The provision of the Logi-AI Suite and associated services will likely impact InnovateTech's revenue streams and cash flows, demonstrating commercial substance.
5. **Probable Collection (ASC 606-10-25-1(e)):** It is probable that InnovateTech will collect substantially all of the consideration. The payment terms are clear, and there is no indication of financial distress from Global Dynamics. The historical success rate of InnovateTech achieving the performance metric with 80% of similar customers further supports the likelihood of collection.

Conclusion:

The contract between InnovateTech Solutions Inc. and Global Dynamics Corp. meets all the criteria under ASC 606-10-25-1 for a valid contract. The parties have approved and are committed to the contract, rights and payment terms are clearly identified, the contract has commercial substance, and it is probable that InnovateTech will collect the consideration.

Issues or Uncertainties:

None identified.

Identify Performance Obligations

Analysis:

The contract between InnovateTech Solutions Inc. and Global Dynamics Corp. includes several promised goods and services. These are:

1. **Logi-AI Suite SaaS License:** A 3-year subscription license for up to 500 users, including standard support and maintenance with monthly updates.
2. **Hardware Provisioning:** Delivery of 200 "OptiScan-7" handheld scanners.
3. **Professional Services:** Implementation, system integration, and on-site user training.

To determine if these are distinct performance obligations, we apply ASC 606-10-25-14 through 25-22.

- **Logi-AI Suite SaaS License:** This is distinct because the customer can benefit from the SaaS license on its own, as it provides access to the platform and includes support and updates. The SaaS license is regularly sold separately, meeting the criteria in ASC 606-10-25-21(a).
- **Hardware Provisioning:** The scanners are distinct because they are transferred to the customer with title and risk of loss, and the customer can use them independently of other services. The hardware is not highly interdependent with the SaaS license or professional services, aligning with ASC 606-10-25-21(c).
- **Professional Services:** These services enhance the functionality of the Logi-AI Suite by integrating it with the customer's ERP system. While the SaaS can be used without these services, the integration significantly enhances its utility. However, the services are not highly interdependent with the SaaS license, as the SaaS can function without them, satisfying ASC 606-10-25-21(b).

The performance bonus and bundle discount do not constitute separate performance obligations. The bonus is contingent on future performance and the discount is a pricing adjustment.

Conclusion:

The contract contains three distinct performance obligations: (1) the Logi-AI Suite SaaS License, (2) the Hardware Provisioning of OptiScan-7 scanners, and (3) the Professional Services for implementation and training. Each is distinct because the customer can benefit from them independently or with other readily available resources, and they are not highly interdependent.

Issues or Uncertainties:

None identified.

Determine the Transaction Price

Analysis:

The transaction price under ASC 606 is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer. In this contract with Global Dynamics, the fixed consideration amounts are clearly outlined. The Logi-AI Suite SaaS License is priced at 240,000 *per year for three years, totaling 720,000*. The hardware, consisting of 200 OptiScan-7 scanners, is priced at a one-time fee of 50,000. *The professional services are also a one-time fee of 75,000*. These amounts are fixed because they are specified in the contract and not subject to change based on future events.

Variable consideration is present in the form of a performance bonus of \$30,000, contingent upon achieving a 15% reduction in shipping costs within the first 12 months. According to ASC 606-10-32-5 to 32-10, variable consideration should be estimated using either the expected value or the most likely amount method. Given InnovateTech's history of achieving this metric with 80% of similar customers, the most likely amount method may be appropriate. However, ASC 606-10-32-11 to 32-14 requires that variable consideration be constrained to avoid significant revenue reversals. The likelihood of achieving the performance metric should be evaluated to determine if the bonus can be included in the transaction price.

The contract includes a 10% bundle discount on hardware and services, which affects the transaction price. The discount does not apply to the SaaS license, which is at its standalone price. This discount should be allocated proportionally to the hardware and services based on their standalone selling prices.

There is no significant financing component in this contract. Payments for the SaaS license are due annually, and the hardware and services fees are due within 30 days of the effective date. According to ASC 606-10-32-15, a significant financing component exists if the timing of payments provides a significant benefit of financing. Here, the payment terms do not indicate such a benefit.

Noncash consideration and consideration payable to the customer are not present in this contract. The transaction involves only cash payments from Global Dynamics to InnovateTech.

Conclusion:

The total transaction price is composed of fixed consideration of 845,000, *which includes the SaaS license, hardware, and professional services, adjusted for the 10%*. 30,000 is subject to constraint evaluation. There is no significant financing component, noncash consideration, or consideration payable to the customer.

Issues or Uncertainties:

The primary uncertainty is the inclusion of the \$30,000 performance bonus in the transaction price. Management must evaluate the likelihood of achieving the performance metric to determine if the bonus should be constrained.

Allocate the Transaction Price

Analysis:

In accordance with ASC 606, the contract between InnovateTech Solutions Inc. and Global Dynamics Corp. involves multiple performance obligations. These obligations, identified in Step 2, include:

- A 3-year subscription license to the Logi-AI Suite (SaaS License)
- Provision of 200 OptiScan-7 handheld scanners (Hardware)
- Professional services for implementation, system integration, and training

Per ASC 606-10-32-31, the transaction price must be allocated to each performance obligation based on their standalone selling prices (SSPs). The SSPs should be determined using observable data, such as market prices or similar transactions, as outlined in ASC 606-10-32-33.

The allocation methodology requires that the transaction price be distributed proportionally to the SSPs of each performance obligation. This ensures that the allocation objective is met, as described in ASC 606-10-32-29. The contract specifies a total transaction price of 365,000, *which includes a 240,000 annual fee for the SaaS license, a 50,000 fee for the hardware, and a 75,000 fee for professional services.*

A 10% bundle discount applies to the hardware and services, but not to the SaaS license, as it is priced at its standard standalone rate. According to ASC 606-10-32-37, the discount should be allocated proportionately to the hardware and professional services obligations, as these are the only components to which the discount applies.

Conclusion:

The transaction price should be allocated to the performance obligations based on their relative SSPs. The 10% discount should be proportionately allocated to the hardware and professional services, as the SaaS license is not discounted. This allocation ensures compliance with ASC 606 guidance.

Issues or Uncertainties:

None identified.

Recognize Revenue

Analysis:

The contract between InnovateTech Solutions Inc. and Global Dynamics Corp. involves multiple performance obligations, each requiring distinct revenue recognition considerations under ASC 606. The primary obligations include the Logi-AI Suite SaaS License, hardware provisioning of OptiScan-7 scanners, and professional services for implementation and training.

1. **Logi-AI Suite SaaS License:** The SaaS license is a subscription service provided over a 3-year term. According to ASC 606-10-25-27, revenue for services provided over time should be recognized over the period the service is delivered. The customer receives and consumes the benefits of the SaaS license simultaneously as InnovateTech performs, satisfying the criteria for over-time recognition. Therefore, revenue should be recognized on a straight-line basis over the 36-month term, as this method best depicts the transfer of service.

2. **Hardware Provisioning (OptiScan-7 Scanners):** The contract specifies that title and risk of loss for the scanners transfer to the customer upon delivery. Per ASC 606-10-25-23, control transfers at the point of delivery, indicating point-in-time revenue recognition. The \$50,000 fee for the scanners should be recognized when the scanners are delivered to the customer's facility, as this is when the customer obtains control.
3. **Professional Services:** These services are a one-time engagement for system integration and training, enhancing the SaaS platform's functionality. Revenue recognition occurs at a point in time upon completion and customer acceptance, as outlined in ASC 606-10-25-23. The \$75,000 fee should be recognized when the customer provides written acceptance, confirming the services are complete.
4. **Performance Bonus:** The \$30,000 performance bonus is contingent upon achieving a 15% reduction in shipping costs within the first 12 months. According to ASC 606-10-32-28 through 32-41, variable consideration should be estimated and included in the transaction price only if it is probable that a significant reversal will not occur. Given InnovateTech's 80% success rate, it is reasonable to include this bonus in the transaction price, subject to reassessment as the performance period progresses.

Conclusion:

Revenue for the Logi-AI Suite SaaS License should be recognized over time on a straight-line basis over 36 months. The hardware provisioning revenue is recognized at a point in time upon delivery. Professional services revenue is recognized upon customer acceptance. The performance bonus is included in the transaction price, contingent on achieving specified cost reductions.

Issues or Uncertainties:

None identified.

PREPARED BY: [Analyst Name] | [Title] | [Date] **REVIEWED BY:** [Reviewer Name] | [Title] | [Date]

This memorandum represents our preliminary analysis based on the contract documents provided. Final implementation should be reviewed with external auditors and may require additional documentation or analysis of specific implementation details.