Navigating Accounting Guidance for Gaming Revenue Recognition

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Accounting for games under Financial Accounting Standards Board (FASB) Accounting Standards Codification 606, *Revenue from Contracts with Customers* (ASC 606)

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Agenda

➢ Subscription revenue

➢ Advertising and sponsorship revenue

➢ License revenue

➢ Prepaid and other gift cards

➢ In-game revenue

    ➢ Direct purchased items

    ➢ In-game currency

    ➢ Contest winnings and other promotions

    ➢ Determining user life

Subscription Revenue

Subscription Revenue

➢ Generally recognized ratably over the life of the subscription

➢ Additional considerations:

    ➢ If the subscription is over a set period (i.e. one-year), is it cancellable at any time? (if so, and the gamer need not continue to pay, or is refunded, this will change the recognition pattern)

    ➢ Are there any additional incentives provided for a long-term subscription?

        ➢ In-game currency – if monthly payments, or a longer-term subscription come with a base amount of in-game currency, consideration should be given as to allocating the transaction price of the subscription between access to the game and the in-game currency provided.

            ➢ Recommendation – establish a price for in-game currency (allowing for discounts and promotions) which can then be used as the basis for the allocation of the transaction price.

        ➢ In-game use items

            ➢ Durable – to be recognized over estimated user life

            ➢ Consumable – to be recognized when used

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Subscription Revenue

Example of allocation of subscription when providing in-game currency:

New game called, "Capital Raises" where players earn points to build their company and try to work towards funding rounds and an eventual exit. They compete on-line with other players for investment dollars. Other players can purchase in-game currency known as "Game Bucks", and invest in companies, trying to earn more money. If you subscribe to the game for one-year, paid up-front, you receive one million Game Bucks. Purchased separately, $1 buys 100,000 Game Bucks. Just like real money Game Bucks don't expire!

Subscription Revenue

➢ By establishing a standalone price, that amount ($1 for 100,000) can now be used to allocate the transaction price. If the subscription is $2/month, or $20 for the 1-year that comes with the million Game Bucks, you would allocate $10 to the Game Bucks and $10 to the subscription.

➢ The Game Bucks would be recorded as deferred revenue until used as investment dollars with another players Company, or use it to start their own. So long as they are still usable Game Bucks, they stay in deferred (and breakage income should be recognized based on estimated user life).

➢ The subscription allocation of $10 would be recognized over the one-year life of the subscription.

Advertising and Sponsorship Revenue

Advertising and Sponsorship Revenue

➢ Dependent on the contract

➢ Ad placement for a period of time is recognized over the period of time

  ➢ If the contract contains clauses on minimum views – consideration should be given if the minimum will be reached before recognizing revenue

  ➢ If the contract pays additional amounts for click-throughs, that revenue should be recognized as the click throughs occur (track your data!)

➢ Ads that only play for click throughs or views, should be recognized as each occur

➢ Practical application of advertising with views and click-throughs:

  ➢ Gather data weekly or monthly and determine if minimums are applicable, and if so were they met, and then recognize revenue based on the available data

➢ Sponsorships will largely work in a similar fashion, but tend to be longer term in nature (over a period of several months or longer

➢ If Sponsorship is for a specific game, consideration should be given as to the life-cycle of the game for recognition of the associated revenue

Advertising and Sponsorship Revenue

Examples:

➢ ABC Ventures wants to advertise in Capital Raises. Each time a player believes they have enough to get an investment and goes to the investment banker screen, ABC Ventures would like an ad to appear in the upper right corner. They will pay $10,000 for the ad to run for one month. They expect a minimum of 20,000 views and will pay an additional $0.10 for every click-through.

➢ Capital Raise Game Company will recognize the $10,000 over the month the ad is running. The company will obtain weekly data reports for click-throughs, and invoice ABC Ventures for them at the end of the month. Although not yet invoiced, all click-throughs are recognized as the data is collected (in this case weekly). This is held as an unbilled receivable until the invoice is generated.

➢ After one week, there were only 2,000 views. The Company now examines if it is possible the minimum threshold will not be reached, and some portion of the $10,000 will become refundable to ABC Ventures. They decide to wait one additional week. Week 2, there are 3,000 views. The pattern looks positive, but even at that growth rate, the minimum may not necessarily be reached. The Company records a discount of $3,000 as estimate and creates a liability to ABC Ventures. At the end of the month, 20,000 views occur, and the Company now removes the liability, recognizing the full $10,000.

License Revenue

License Revenue

➢ Dependent on the contract

➢ Generally, revenue under license arrangements has multiple components

➢ Up front fee that provides use of the name over a period of time

  ➢ This is generally recognized over the life of the contract

➢ Royalty payments for revenue of the licensee

  ➢ This is specifically noted in ASC 606 as being recognized when the underlying sale occurs

  ➢ Practically speaking, when information is provided by the licensee as to what was sold, and royalties owed (often monthly), revenue is then recognized.

  ➢ Accounting reminder: Ensure proper consideration is given to completeness of the license revenue. This is an important part of internal controls over financial reporting.

License Revenue

Example of License Revenue:

➢ Capital Raises is booming! So much so that XYZ Merchandising calls and would like to sell Capital Raise merchandise. Capital Raise Game Company agrees, and they sign a 3-year exclusive license agreement for $100,000. The agreement also calls for 2% of all revenue from Capital Raise Merchandise to be paid to Capital Raise Game Company.

➢ The $100,000 payment is recognized over the life of the agreement, or three years. Consideration can be given is the expected life-cycle of the game is shorter than 3-years for accelerated recognition, but for a new game that would be considered difficult to support as XYZ seems to believe they will benefit over the 3-year term of the agreement.

➢ On a monthly basis, Capital Raise receives a report from XYZ detailing merchandise sold, and amount of royalty owed. This amount is recognized as revenue.

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License Revenue

Example of License Revenue:

➢ Capital Raise ensured its License agreement contained a clause where they have the right to audit the records of XYZ to determine that the correct amount was paid. After a year, Capital Raise invokes this right and determines that XYZ should have paid an additional $10,000 in royalties. This amount is recognized at the conclusion of the audit.

Prepaid and other gift cards

Prepaid and other gift cards

➢ Generally, prepaid and other gift cards are initially recorded as deferred revenue when cash is received.

➢ What the card is used to purchase will determine the revenue recognition pattern

➢ For purchases of in-game currency, it simply moves to a different type of deferred revenue, in-game currency deferred revenue, and is recognized based on the section of this presentation.

➢ For purchases of a game, it will depend if it is a subscription for the game, or just the purchase of a game that is the customers to use indefinitely.

    ➢ Subscriptions will follow the subscription model of over time recognition

    ➢ One-time purchases, the revenue is recognized when the download occurs

➢ What about cards that never get used?

    ➢ Breakage for a prepaid or gift card can only be taken if the applicable state is favorable regarding escheatment laws. Once the gamer purchases the game and/or in-game currency, escheatment will mot likely no longer apply.

➢ Prepaid or gift cards sold at a discount should result in a contra-liability that will be relieved through a discount to revenue.

Prepaid and other gift cards

Example of prepaid and other gift cards:

➢ Capital Raise begins selling through its website prepaid cards that can be given as gifts for Game Bucks. The cards are through a specific subsidiary in Alabama, a favorable state for escheatment laws, which also happens to be one of the states the Company has a physical presence in, and therefore is able to take breakage on unused cards.

➢ As each card is used for Game Bucks, the deferred revenue is moved from gift card deferred revenue to Game Bucks deferred revenue.

➢ Since the cards are in a favorable state, the Company also takes breakage income for the estimate of purchased cards that will never be used.

In-Game Revenue

In-Game Revenue – Direct purchase of items

➢ Items that are directly purchased are recognized depending on the nature of the item, and when it is used.

➢ Items that are consumable goods are recognized when the goods are used. When initially purchased, it is considered deferred revenue until used.

➢ Durable goods depend on the duration of the good (permanent or temporary)
  ➢ Temporary goods such as a magical torch that lasts for 10 days, is recognized over that temporary period.
  ➢ Permanent goods such as a new sword that the character will have when playing the game will be recognized based on the expected user life.

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In-Game Revenue – Direct purchase of items

Example of direct purchased items:

➢ Jack is enjoying Capital Raises. He decides that the $10 for the one-time use "Instant Funding" token is worth it. He purchases the token and uses it the next day.

➢ When Jack uses the token and receives Game Bucks for his company in the game, Capital Raise recognizes the revenue.

➢ Jack then sees there is a permanent token called "Successful Entrepreneur". This token gives Jack a bonus when competing for investment Game Bucks in the game. It's a permanent item that stays with Jack so long as he is playing the current character. Jack purchases the token, and then defeats his opponents for the next funding round!

➢ Capital Raise has estimated the average user life for the game to be 10 months. They therefore recognize the Successful Entrepreneur token over 10 months.

In-Game Revenue – In-Game currency

➢ Purchased in-game currency, whether directly purchased or through a prepaid or gift card is deferred revenue until used. This is because the game has a future performance obligation for the in-game currency.

➢ Breakage should be based on historical results, or for a new game, an estimate based on other similar games, or industry examples.

➢ Revenue is not recognized until the currency is used to purchase something in-game.

➢ Once purchased, the revenue recognition follows the previous section outlining direct purchase of items.

In-Game Revenue – In-Game currency

Example of in-game currency:

➢ Jill is interested in buying some tokens for her company in Capital Raises, so she purchases one million Game Bucks for $10. She then buys the Certified Investor token (permanent item) for 500,000 Game Bucks.

    ➢ This is a permanent token, so the $5 for 500,000 Game Bucks is recognized over the estimated user life of 10 months.

➢ Jill then decides to buy the one-time use Perfect Presentation token to help her secure her next round of funding for 300,000 Game Bucks.

    ➢ The revenue for 300,000 Game Bucks ($3) is recognized as the token is used,

➢ The remaining 200,000 Game Bucks ($2), stays in deferred revenue, and is part of the pool considered for breakage revenue.

In-Game Revenue – Contest winnings and other promotions

➢ An example would be the funding rounds in Capital Raises discussed throughout the presentation. In the example of this game, a player wins a funding round and receives 100,000 Game Bucks for winning the round. Capital Raise Game Company never collected the cash of $1 for these Game Bucks.

➢ The Game Bucks are in deferred revenue, but since they were not paid, there is also a contra-liability. When the Game Bucks are used, gross revenue is recognized, but so is a discount to revenue. The result is net zero revenue. Wining a contest is great, and although often considered part of marketing a game, it is not generally considered an expense.

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In-Game Revenue – Contest winnings and other promotions

➢ The exception to this rule is if contestants paid to enter the contest.

➢ For example, if 10 gamers playing capital raise all put in 200,000 Game Bucks each, and the winner got the 2 million Game Bucks, the 2 million Game Bucks would be deferred revenue, but there would be no contra-liability as this was cash received by Capital Raise Game Company and therefore will turn into revenue once the winner uses those Game Bucks.

   ➢ The 2 million Game Bucks won is also subject to potential breakage income.

In-Game Revenue – Contest winnings and other promotions

➢ Promotional giveaways receive similar treatment. Unless there is an identifiable cost associated with the Game Bucks provided, they generally follow the same pattern.

➢ An identifiable cost however can mean things such as bartered ad space, sponsorship of an event or other marketing costs.

➢ As the Company Is receiving consideration in the form advertising, this would be revenue and marketing expense.
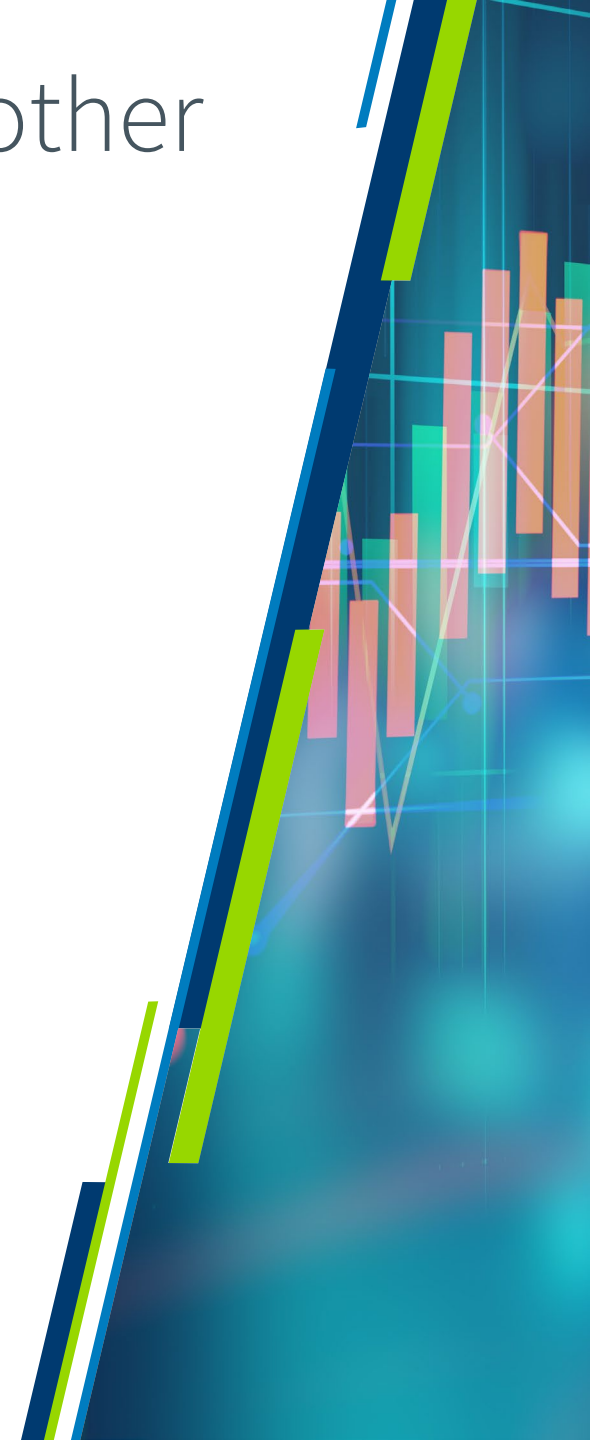
In-Game Revenue – Contest winnings and other promotions

Example of other promotions:

➢ JKL media decided for their next event they wanted to give away Game Bucks to some attendees. They agreed with Capital Raise Game Company to provide $20,000 worth of ad space for one billion Game Bucks.

➢ An important fact for this example is that the Game Bucks under normal circumstances would only be worth $10,000. However, as the consideration provided for these is $20,000, that is the value for this set of Game Bucks. It should be tracked separately as every $1 of normal value from this agreement, will result in $2 of revenue.

➢ The event occurs, and the Game Bucks are given out. Capital Raise Games received the $20,000 worth of advertising. The initial entry is a debit to marketing expense, and a credit to the Game Bucks liability. This is because the expense has been incurred, but the revenue can't be recognized until the Game Bucks are used (or breakage income is taken).

In-Game Revenue – Estimating user life

➢ Game user lives vary significantly depending on factors such as type of game, what medium is used for the game, and popularity of the game.

➢ User lives can run from as short as one month for certain mobile games to as much as 27 months (per the 2024 Roblox 10-K filing).

In-Game Revenue – Estimating user life

		Total Downloads per Month	Total Months Used	Average User Life
Number of Users		1,000		
Average Total Days		99.8		
March	3	60	412	6.87
April	4	90	542	6.02
May	5	107	614	5.74
June	6	111	552	4.97
July	7	93	410	4.41
August	8	103	421	4.09
September	9	109	395	3.62
October	10	118	316	2.68
November	11	108	210	1.94
December	12	101	101	1.00

Questions

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Bradley (Brad) Hausman, CPA, has more than 19 years of accounting, auditing, and business advisory experience serving privately held and public companies in a variety of industries including technology (with an emphasis in Gaming), hospitality (restaurants and tour and travel), and manufacturing and distribution. As a partner in the firm's Technology, Manufacturing, Hospitality and Technology practices, he focuses on working with middle market companies in those industries.

Brad has been a part of auditing publicly traded companies throughout his career in accounting including technology, restaurants, a healthcare service provider, and a medical device company.

Areas of expertise
Industries: Technology (Gaming), Hospitality, Manufacturing & Distribution
Services: Accounting and Assurance, Accounting Services, Attest & Audit

Experience and credentials
- Assisted in the development of CohnReznick's testing methodology for auditing revenue for technology (including gaming), restaurants and other industries, as well as leading the effort to develop templates for auditing of technology companies, manufacturers, distributors, restaurants and retail clients.
- Leads various trainings including training partners, managers, and team members across the firm on auditing methodologies, revenue recognition, and lease accounting.