



## FULFILLMENT COSTS

Fulfillment costs are costs that are (1) directly related to a specific contract, (2) generate or enhance a resource that is used to fulfill a performance obligation, and (3) are recoverable under the contract. However, if any of these costs are addressed by other standards (e.g., inventory), that guidance must be applied. In addition, some fulfillment costs may fall under capitalized costs.

Examples of fulfillment costs include

- ▶ Certain costs that are incurred prior to the transfer of control of goods or services to the customer, for example, insurance/surety bonds, engineering and design, mobilization costs of equipment and labor to and from a job site, costs for production equipment relating to the contract, costs incurred to acquire or produce goods in excess of contractual requirements in anticipation of follow-on orders for the same item, direct labor costs related to the contract.
- ▶ Incremental costs, that is, costs incurred in obtaining the contract that would not have otherwise been incurred.

Costs that do not meet the definition of fulfillment costs are expensed as they are incurred. Examples of such costs include general and administrative costs not specifically tied to the contract and the cost of wasted materials, labor or other materials not reflected in the price of the contract.

## HOW THIS RULE WORKS

- ▶ Certain contract fulfillment costs that are not governed by other standards (e.g., inventory) may be capitalized on the balance sheet.

### SUCH COSTS MUST

- Directly relate to a contract or an anticipated contract
- Be specifically identifiable
- Generate or enhance resources that will be used in satisfying (or continuing to satisfy) future performance obligations
- Be recoverable

- ▶ Any costs that are capitalized must be amortized over the period during which control was transferred to the customer.
- ▶ Fulfillment costs must be deferred and amortized to the contract as transfer of control occurs.

**This determination requires the contractor to use a significant amount of judgment. To avoid making an error, be sure to review your determination with a professional with expertise in ASC 606.**

## HAVE QUESTIONS?

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