The Main Dish

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Loyalty programs: new revenue recognition standard impact

By Jonathan Poppel, CPA

Like many restaurant owners, you may offer a program to build customer loyalty and increase sales volume. For example, a program where customers accumulate points as they spend money at your restaurant which they can redeem for free items or discounts. These programs are impacted by the new revenue recognition standard and you're going to need to make some accounting changes.

Under the new standard, points earned from loyalty programs are considered customer options that provide material rights to customers. Accordingly, points earned should be accounted for as a separate performance obligation. This means that if your restaurant offers a loyalty program, you will allocate a portion of your restaurant sales to this separate performance obligation. This amount will be recognized in revenue as the points are redeemed by customers or when the points expire. Similar to gift card accounting, you will need to consider the expected breakage. For loyalty programs, breakage relates to the amount of points that go unused by customers or expire. Here's an example of how to account for restaurant sales to customers under your loyalty program:

- Your restaurant has a customer loyalty program that rewards customers with one loyalty point for every $15 of purchases. Upon the accumulation of 10 points, the customer can redeem for $10 off the customer's restaurant bill. Points expire one year from the date earned.
- During the month, restaurant sales to loyalty program customers are $1,200,000 and those customers earn 80,000 points that are redeemable for future restaurant visits.
- Your restaurant estimates 90% of the points to be redeemed, resulting in a standalone selling price of $.90 per point (totaling $72,000) based on a likelihood of redemption.

The allocation of the transaction price ($1,200,000) to the restaurant sales and the points is as follows:

Restaurant sales ($1,200,000 x ($1,200,000 / $1,272,000))	$ 1,132,075
Points ($1,200,000 x ($72,000 / $1,272,000))	$ 67,925
Total Transaction Price	$ 1,200,000

If, during the month, customers redeem 15,000 points, you would recognize revenue for the loyalty points of $14,150 (15,000 points / 72,000 points x $67,925). The contract liability would be reduced by the $14,150, resulting in a contract liability balance of $53,775 for the unredeemed points at the end of the month. This amount would be reflected as an obligation (i.e. liability) on your balance sheet at month-end.

This is a simplified example of how the accounting for loyalty programs works. Going forward, you would likely adjust the points obligation liability at month-end based upon the amount of loyalty program points that are outstanding. Expected breakage would also need to be regularly reviewed and adjusted, if necessary, based upon actual point usage and expiration rates.

If you have any questions, Jonathan can be reached at (480) 839-4900 or JonathanP@hhcpa.com.

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Updated tip pooling laws
By Kelly Lynch, CPA

In case you missed it, this past spring President Trump signed the omnibus budget bill that contained a provision which would allow tips to be shared and pooled between all employees. This effectively rolls back the Department of Labor rule adopted by President Obama in 2011 that attempted to prohibit back-of-the-house staff from participating in tip pools in restaurants where employers did not take a tip credit. This is a significant victory for the industry as the exclusion for the back-of-the-house employees, like dishwashers, cooks and other kitchen staff, has been lifted.

What is tip pooling?

Tip pooling is collecting all tips from directly tipped staff and putting them into one large "pool." The tips are then redistributed among a larger group of employees. Tip pooling ensures that all staff members are fairly compensated for their work, especially when there are multiple services being rendered and single points of payment.

Again, employers who pay the full Fair Labor Standards Act (FLSA) minimum wage are no longer prohibited from allowing employees who are not customarily and regularly tipped – such as cooks and dishwashers – to participate in tip pools. Furthermore, as it relates to a supervisor or manager, if an employee earns most of their pay through tips, but also has a limited supervisory role, they are still allowed to participate in a tip pool.

Best practices

As an employer, you should consider taking the following steps to limit liability on tip pooling claims:

- A mandatory tip pool can include all line employees, even those with limited customer contact – the law now recognizes these employees as being part of the chain of service for the industry.
- If a mandatory tip pool is instituted, the employees with the greatest amount of customer interaction should get the largest percentage of the tips. It is important to make sure the tip pool is distributed to participating employees in a reasonable manner.
- It is illegal for the employer to share in the tip pool and, therefore, do not distribute any portion of a tip pool to any owner, even if they provide direct table service and/or the tip was left by the patron specifically for that individual.

It is important to review your current tip pooling arrangement, if you have one, and revise it as needed to comply with the new rules. For more specific questions about tip pooling policies, consult with legal counsel who understands both the industry and wage and hour issues given your specific circumstances and policies.

If you have any questions, Kelly can be reached at (480) 839-4900 or KellyL@hhcpa.com.

Henry+Horne has performed several audits of our annual financial statements, and each year they have submitted the reports on or before deadline. All members of the engagement team are very knowledgeable, extremely responsive and professional.