What is Deferred Revenue?

Last Modified on 09/13/2024 6:13 pm EDT

In accrual accounting a company recognizes revenue when they earn it, not when they create the invoice for it.

For example, let's say a customer is billed annually in January for a 100.00 monthly RMR line. In this case the invoice would be 100 per month, for 12 months, for an invoice total of 1,200. The company is going to earn that 1,200 by monitoring its customer's alarm system every month for the next 12 months.

If we are currently in January, then 11 of those months have not happened yet, and the monitoring for those 11 months hasn't happened yet. This means 100 of the invoice amount can go to revenue, because the company earned it, by monitoring the alarm system during January. The remaining 1,100 must go to a holding account, and wait to be recognized as revenue slowly over time, as the company performs the service it was paid for.

The holding account the money sits in, is called deferred revenue. In other words, revenue that has been deferred until the month of service.