ACCT 352 Research Case – Spring 2021

Crimson Tide Shipping (“Crimson”) provides domestic and international transportation and

logistics services to customers. The company contracts shipping vessels, trucks, and aircraft to

provide regional, long-haul, and international shipments of customer goods. Crimson has entered

into the following contracts:

In March 2019, Crimson entered into a revenue contract with a customer, Matador

Manufacturing (“Matador”), in which Crimson would be the exclusive shipper of Matador’s

products between Shanghai and Los Angeles. Crimson’s contract with Matador is effective on

July 1, 2019. Before signing the contract with Matador, Crimson did not operate the ShanghaiLos Angeles route,

and to satisfy the contract with Matador, in April 2019, Crimson leases a

cargo ship from Buckeyes Vessel Manufacturing (“Buckeyes”), which commences on July 1,

2019.

Because the shipping route is new, on July 1, 2019, (1) Crimson has no other customers to

deliver goods on the Shanghai-Los Angeles route and (2) because of operational costs, Crimson

does not have alternative uses for the leased cargo ship.

Crimson adopted ASC 842, Leases, on January 1, 2019.

The following are relevant facts about Crimson’s revenue contract with Matador, and Crimson’s

lease with Buckeyes.

Crimson’s Revenue Contract with Matador

 The revenue contract’s stated term with Matador is for one year.

 Matador can renew the contract annually for up to four additional years. Therefore, the

revenue contract can extend to five full years.

 Matador pays a significant up-front nonrefundable fee for the initial one-year term; the

same amount is due at the beginning of every renewal period.

 Matador can cancel at any time without incurring a penalty outside of forfeiting any upfront nonrefundable fees

already paid or owed at the beginning of the initial contract term

and any and each renewed period.

 Although the contract is new, Crimson and Matador have entered into similar

arrangements with similar terms and historically, Matador has renewed for one or more

years.

 Crimson appropriately concludes that (1) the revenue contract meets the scope of, and

criteria in, ASC 606, Revenue From Contracts With Customers, and (2) the contract term

for its revenue contract with Matador is one year.

Crimson’s Lease with Buckeyes

 The contract between Crimson and Buckeyes contains a lease under ASC 842.

 Rental payments are at market and fixed each year.

 To mitigate risks, Crimson negotiated the lease period and renewal options to mirror

those of Crimson’s revenue contract with Matador. As a result, the fixed, noncancelable

term of the lease is one year, and Crimson can renew annually for four additional years

(i.e., up to five full years).Crimson believes that since Matador can terminate the revenue contract after one year

(even

though Matador may need to ship products for longer than a year and has historically renewed

under other similarly structured contracts), it is uncertain whether Matador will renew the

revenue contract. Because of this uncertainty, Crimson believes that the renewal options related

to the lease are not reasonably certain at the commencement date of the lease.

As a result, Crimson concludes that the lease term for its lease contract with Buckeyes is also one

year.

Required:

1. Do you agree with Crimson’s conclusion that the lease term for the cargo vessel is one

year because the revenue contract is for one year?

2. What factors should Crimson consider in supporting its conclusion related to the lease

term?

Additional Facts

On December 1, 2019, Crimson entered into a shipping contract with Redhawks Manufacturing

Company (“Redhawks”) to ship Redhawks’ products between Shanghai and Los Angeles. The

contract with Redhawks commences on January 1, 2020, and on the basis of Crimson’s

evaluation of its enforceable rights and obligations in the contract with Redhawks, Crimson

concludes that term of the revenue contract with Redhawks is for a period of two years. Further,

Crimson concludes that (1) because of its contract with Matador and Redhawks, it would not be

operationally feasible to deploy the leased cargo vessel on other routes; (2) the cargo

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have sufficient capacity to service both Matador and Redhawks; and (3) the leased asset is

needed for Crimson to perform under its revenue contract with Redhawks (because of economic

reasons that would not allow Crimson to use another vessel).

Required:

3. Should Crimson reassess the lease term of the cargo vessel? If so, why?

Analyze the above and prepare a 2-page report (font 12 of Times New Roman; short

answers with bullet points are encouraged) addressing the three questions.