Research Question Solution

Until 2021, Fabulous Fruit should not recognize revenue from the sale of peaches that are harvested from the newly-planted peach trees and sold at local farmers' markets. The net proceeds from sales during 2019 and 2020 should be deducted from the capitalized costs of the trees until commercial production begins in 2021 (FASB, 2018, ASC para. 905-360-25-2). In 2021, Fabulous Fruit will begin selling these peaches to commercial canning companies and shall recognize revenue at that time.

Excerpts (not required to be included in this assignment)

905 Agriculture
360 Property, Plant, and Equipment
25 Recognition

25-2 Trees and vines may be planted and brought to production by the producer or on a contract basis. The young trees and vines are usually purchased as nursery stock and transplanted into the orchard or vineyard in the desired pattern. Cultural costs during the development period, including stakes and wires, grafting, and labor for pruning and forming, shall be capitalized. Net proceeds from sales of products before commercial production begins shall be applied to the capitalized cost of the plants, trees, or vines.

Note to students: This standard states "Net proceeds from sales of products before commercial production begins shall be **applied** to the capitalized cost of the plants, trees, or vines." Always analyze what a confusing word means and explain it to the client. Eventually the client will ask you for an explanation if it is not understood. Never expect the client to figure it out. The word "applied" should be interpreted as decreasing the capitalized cost. Many students incorrectly interpreted this word to mean "increase" the capitalized costs. Sometimes a word such as this one can have more than one meaning. In such cases, you should test the logic of your interpretation by using journal entries or T-accounts. For example, when the costs of the trees were incurred, the journal entry would have looked something like the following:

Trees (capitalized costs)	xxxxxx	
Cash/Accounts Payable, etc.		xxxxxx

When the peaches are sold at the farmers' markets prior to the beginning of commercial production, the following journal entry for the net proceeds should have been recorded:

Cash/Accounts Receivable	xxxxxx	
Trees (capitalized costs)		xxxxxx

For those of you who thought the capitalized costs should have been increased, try recording a journal entry. If you debit Trees to increase the capitalized costs, what would you credit? It can't be a revenue account. The standard prohibits that. It certainly wouldn't be a liability.

Another logical question to ask yourself is if the peaches are sold, shouldn't that increase net income? The answer is yes. But not on the revenue side according to the standard. The trees are classified as depreciable property, plant, and equipment. That's right – they are depreciable assets just like equipment. By decreasing the capitalized cost, the future depreciation expense will be lower. Therefore, lower depreciation expense results in higher net income.