

Agriculture

IAS 41

IAS 41 Agriculture

- ✓ *Agricultural activity*
- ✓ *Biological assets*
- ✓ *Agricultural produce*



Overview of IAS 41

Issued: issued in 2000, followed by amendments

Effective date: 1 January 2003

What it does:

- IAS 41 applies to biological assets, agricultural activity and government grants related to biological assets measured at fair value less costs to sell.
- It Standard ***provides definitions*** of:
 - Agricultural activity (and its examples: raising livestock, cropping, cultivating orchards and plantations, etc.),
 - Biological transformation,
 - Biological asset (living animal or plant),
 - Bearer plant,
 - Agricultural produce (harvested product of entity's biological assets), etc.

- IAS 41 sets **3 recognition criteria** for biological asset or agricultural produce:
 - Control of an asset by the entity as a result of past events;
 - Probable future economic benefits will flow to the entity; and
 - Fair value or cost of the asset can be measured reliably.
- A biological asset shall be **measured on initial recognition** and at the end of each reporting period at its **fair value less costs to sell**.

- **Agricultural produce** harvested from an entity's biological assets shall be measured at its fair value less costs to sell **at the point of harvest**.
- IAS 41 then deals with **gains and losses**, inability to measure fair value reliably, provides **rules for government grants** related to biological assets.
- IAS 41 requires number of **disclosures**.
- **Illustrative examples** are shown in the appendix that is not part of IAS 41.

Top 3 Questions about IAS 4I Agriculture



Question #1: Is it agriculture?

The first and primary question when dealing with living plants and animals is – ***what is agricultural activity?***

- It is the management of the biological transformation (e.g. growth) of biological assets for (IAS 41.5):
 - Sale, or
 - into agricultural produce, or
 - into additional biological assets.

You have to make your best effort to answer that question correctly, because the accounting and reporting depends on it.

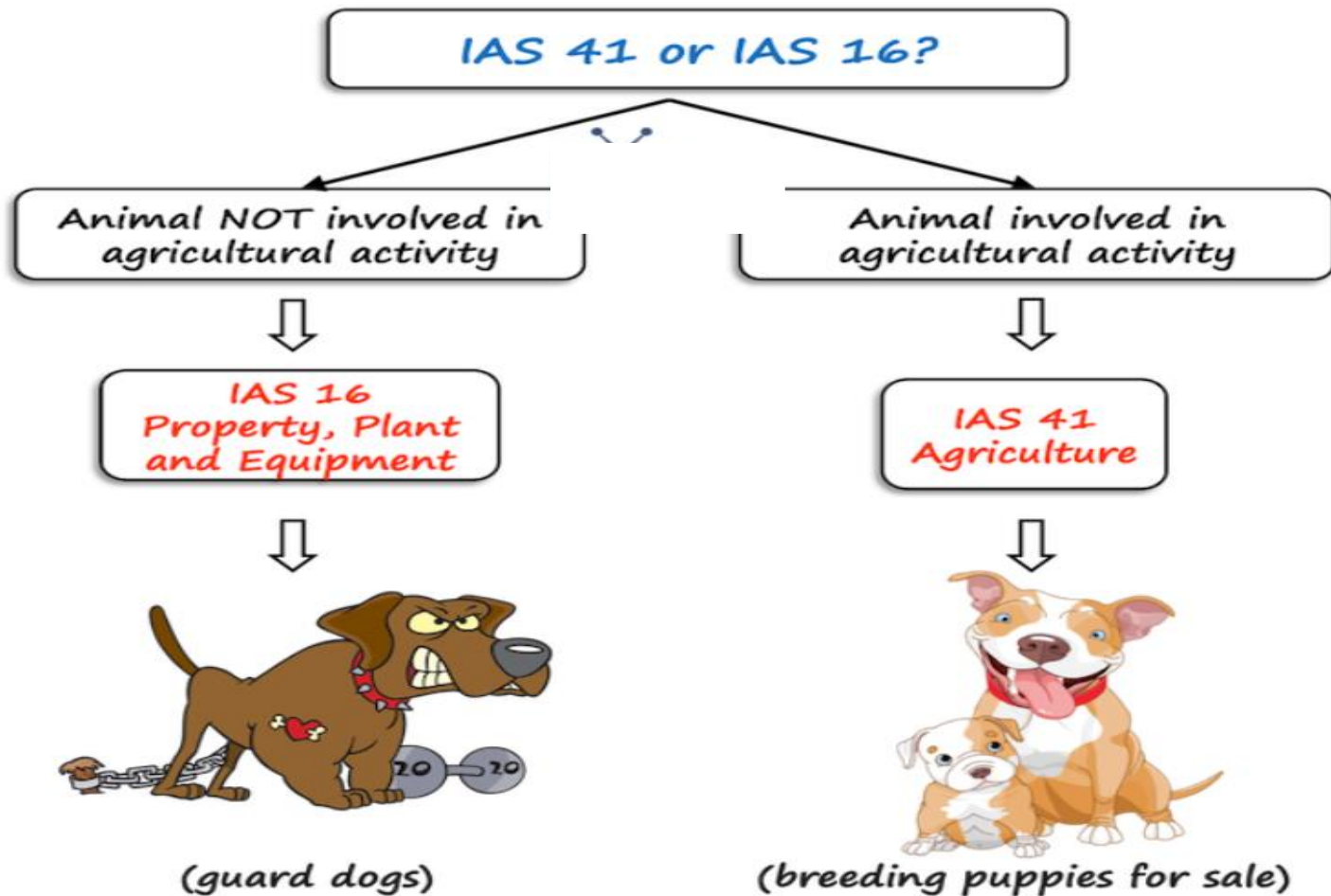
- Why?

Imagine you have a dog.

Logically, it is a living animal, and therefore it is a biological asset. You might think: “well, biological assets are governed by IAS 41, so I need to measure the dog at fair value at the end of each year”.

Not so fast.

- Why do you have that dog?
- Is it a guard dog, protecting your property and barking at everyone passing by?
- If yes, then you should NOT apply IAS 41, but [IAS 16 Property, plant and equipment](#) and measure the dog at cost less accumulated depreciation.
- The reason is that protecting the property is NOT an agricultural activity and IAS 41 does NOT apply.
- Or, do you have that dog in order to produce and raise puppies and sell the puppies?
- In this case, IAS 41 applies, because breeding and selling puppies is an agricultural activity.



So, if you think that OK, I'm not a farmer, so I don't need to bother with IAS 41, you might be surprised where the agriculture can hide.

Just a few examples:

- ***Pharmaceutical companies***

Some pharma companies grow their own plants in order to produce drugs. Yes, this is an agricultural activity and IAS 41 applies.

- ***Diary producers***

If a company grows its own bacteria and cultures and then adds them to its yoghurts, well – this is an agricultural activity and IAS 41 applies.

- ***Jewelry producers***

Some big jewelry producers produce their own pearls by planting foreign objects (such as pieces of shells or parasites) into the soft bodies of living oysters. Then, the oyster produces a pearl by secreting crystalline substance around the object to protect itself. Yes, this is an agricultural activity and IAS 41 applies.

On the other hand, not everything involving living plants or animals is agricultural activity.

Again, few examples:

- **ZOO**

The main purpose of the ZOO (and safari, recreational park, riding hall, etc.) is to make money from showing the animals off to the public – this is NOT an agricultural activity and IAS 41 does NOT apply (IAS 16 does).

Yes, animals living in the ZOO sometimes pair and produce a baby – but if it's a natural process, not managed by the ZOO, it is NOT an agricultural activity.

The situation would be different when the ZOO would implement an active program of reproduction and managed that program. In this case, breeding animals would NOT be an incidental and ZOO would have to apply IAS 41.

- ***Fishing***

All fishermen catching fish in the ocean can breathe with relief. If you are NOT actively farming fish, but you're merely harvesting the fish from the ocean, it's NOT an agricultural activity.

The reason is that fish grew naturally in the ocean, which was NOT an agricultural activity.

The same applies for hunting and other similar activities of harvesting biological assets from nature.

- ***“Working animals”***

When you hold an animal primarily to do some work, such as cart-horses, guard dogs, elephant taxis, etc., then you do NOT apply IAS 41, because all these activities do NOT represent biological transformation.

Instead, IAS 16 is the right way to go.

Question #2: Is it a biological asset?

Very common **misconception** in the agriculture accounting is the belief that everything coming out of agriculture is a **biological asset**.

Not true.

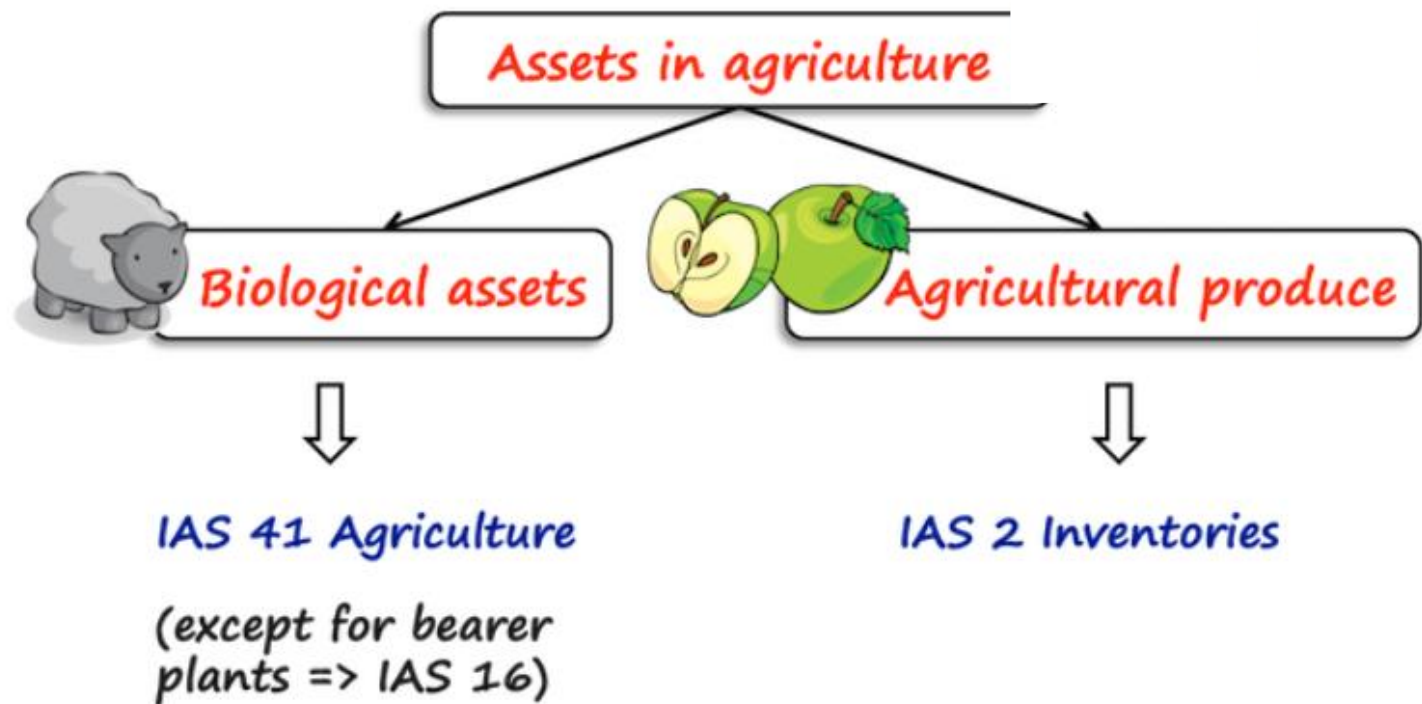
Biological assets are only living plants and animals.


The harvested products of biological assets are agricultural produce.

Apples, palm oil, pearls, milk, coffee beans, tea leaves – all this is agricultural produce.

Why do we bother?

Well, once you detach the agricultural produce from a biological asset, in other words – once you harvest the produce, it becomes your inventories and you apply IAS 2 Inventories.






At the moment of harvest, you should measure your new inventories at their fair value less costs to sell and subsequently, you measure them under IAS 2 at lower of cost and net realizable value.

You do NOT remeasure agricultural produce to fair value less cost to sell.

Question #3: Are biological assets always measured at fair value less costs to sell?

- No, they are not.
- It is true that the general rule in IAS 41 Agriculture is to measure all biological assets at ***fair value less costs to sell***.
- However, there are few exceptions:
- The biological asset is ***NOT a part of agricultural activity***. I've explained it above – guard dogs, fish caught in the ocean, etc.
- The biological asset is ***a bearer plant***. This is a relatively new thing in both IAS 41 and IAS 16 adopted in 2014.
- A bearer plant is a living plant used in production or supply of agricultural produce that is expected to produce for more than 1 period.



The examples are fruit trees, oil palms, vines etc. As it was difficult and impractical to set the fair value of these assets at the end of each reporting period, they were taken out of IAS 41's scope.

So, you can keep these assets at cost less accumulated depreciation under IAS 16.

Careful! – this is only about plants, not animals. So, if you own expensive dogs and use them to breed new dogs, then sorry, it's **NOT** a bearer plant.

3. The fair value is not reliably measurable

When the fair value cannot be measurable, you can measure the asset at its **cost less accumulated depreciation**.

However, this is almost never relevant and IAS 41 says that the fair value CAN be measured reliably for biological assets.

Also, this exemption is available ONLY at initial recognition, never later. So, if you received the biological asset as a gift and market prices are not available, you would be able to use cost model.

Other situations are highly unlikely.



Fair value



Costs to sell


At each reporting date

EXCEPT FOR:

- ✓ If there's no agricultural activity
- ✓ If asset = bearer plant
- ✓ If fair value not available

How to Account for Subsequent Expenditures in Agriculture





The standard IAS 41 Agriculture prescribes measuring all biological assets at fair value less costs to sell (with exceptions), while all the changes in fair value are recognized in profit or loss.

Here, one significant question arises: How should you account for expenditures that you incur during the year in relation to these biological assets?

Food, vaccinations, veterinary expenses, fertilizers, pesticides...?

- The standard IAS 41 Agriculture **is silent** on this topic. There are no exact rules on how to present these costs.
- But, the ***presentation of the individual expenses in your profit or loss is totally affected*** by the way of how you treat the subsequent expenditure.

Select the accounting policy

In any case, it is YOU who need to set the accounting policy of treating the subsequent expenditure.

- Basically, you have 2 options:
 - Put all subsequent expenditure in profit or loss directly, or
 - Capitalize the subsequent expenditure in the carrying amount of your biological assets

How to account for expenses in agriculture?



Develop **your own** accounting policy!



Recognize all expenses
in PL directly



Capitalize expenses in
the carrying amount of
a biological asset

Option #1: All expenses in profit or loss

This is very simple and very easy way of doing the things.

The problem is of this is that, It would show big expenses in your profit or loss statement and on the other hand, you would show big increase in fair value of your biological assets.

What's wrong with that?

Well, the fair value of your biological assets increases not only due to external market changes, but also due to your activities like feeding the animals, taking care of them etc.

If you present all expenses in profit or loss, you are effectively presenting the increase in fair value in one bunch regardless its source or reason.

Sure, for some assets, you need to add additional disclosures about the fair value change due to price change and physical change – but this disclosure is just encouraged, not obligatory.

Option #2: Capitalize expenses in the carrying amount of an asset.

- Under the first option, you would add the expenses to the carrying amount of the biological asset.
- This way, you do not show big expenses for agricultural activity in your profit or loss, and also you show smaller increase in fair value of your biological assets.
- In turn, this method might reflect the fair value changes better than the first method, but it is more demanding and challenging.

Example: expense vs. capitalize

Let's say the fair value of your herd of sheep was TZS 1,000,000 at the end of year 1. In the year 2, you spent TZS 200,000 for the sheep food supplements, vet and other living and breeding expenses. The fair value of your herd is TZS 1,500,000 at the end of the year 2.

Required: Show the accounting treatments under methods 1 and 2.

Accounting #1 – all expenses in profit or loss

The journal entry for the subsequent expenses is:

Debit Profit or loss – operating expenses: TZS 200,000

Credit Suppliers / Bank account: TZS 200,000

The journal entry to remeasure the carrying amount of sheep herd to fair value less cost to sell at the end of year 2:

Debit Biological assets: TZS 500,000 (TZS 1,500,000 – TZS 1,000,000)

Credit Fair value change in profit or loss: TZS 500,000

Here, the net effect in profit or loss is TZS 300,000 which is a gain from remeasurement of 500,000 less the expenses of 200,000.

Accounting #2 – expenses are capitalized

The journal entry for the subsequent expenses is:

Debit Biological assets – sheep herd: CU 200

Credit Suppliers / Bank account: CU 200

The journal entry to remeasure the carrying amount of sheep herd to fair value less cost to sell at the end of year 2:

Debit Biological assets: TZS 300,000 (TZS 1,500,000 – TZS 1,200,000)

Credit Fair value change in profit or loss: TZS 300,000

The net effect in profit or loss is TZS 300,000 which is just gain from remeasurement.

- So it's the same, but the presentation is different.

This table summarizes the impact on profit or loss

	Expense	Capitalize
FV change	500,000	300,000
Operating expenses	-200,000	0
Net effect on P/L	300,000	300,000



END OF IAS 41

Any questions?