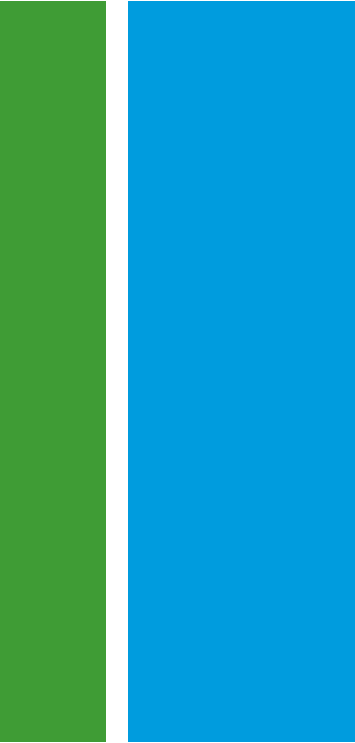


# THE POWER OF BEING UNDERSTOOD

AUDIT | TAX | CONSULTING



---

This slide presentation has been prepared for general guidance only, and does not constitute professional advice. You should not act upon the information contained in these slides without obtaining specific professional advice. Accordingly, to the extent permitted by law, RSM Eastern Africa (and its employees and agents) accept no liability, and disclaim all responsibility, for the consequences of anyone acting, or refraining from acting, in reliance on the information contained in these slides or for any decision based on it, or for any consequential, special or similar damages even if advised of the possibility of such damages.



# IAS 41 – AGRICULTURE

## PRACTICE ISSUES

By Simon Fisher

# Agenda

---

- IAS 41 in a nutshell
- What is a biological asset?
- Fair value of bearer plants – before the amendment
- Fair value of growing produce

# IAS 41 in a nutshell - before

---

Biological assets have to be measured at fair value.

There was only one problem in implementing this:

- How do you measure the fair value of biological assets?

# IAS 41 in a nutshell - after

---

Biological assets other than bearer plants have to be measured at fair value, but growing produce now has to be measured at fair value.

There are only two problems in implementing this:

- How do you measure the fair value of growing produce?
- How do you measure the cost of the bearer plant?

# What is a biological asset?

---

- **Biological assets** are living animals or plants (huge diversity – avocados to zebus):
  - living animals such as chickens, cows, crocodiles, fish
  - plants such as cereals, flowers, vegetables, fruit trees
  - plantation crops such as tea, sugar cane, sisal, trees (for timber)
- Standard should be applied to account for the biological assets, ***when related to agricultural activity.***

# Quiz

---

Which of the following fall within the scope of IAS 41?

- Trained guard dogs used by a security company
- Horses used to provide horseback safaris
- Dogs being bred to be sold as guard dogs
- Lions in a zoo
- Footballers under contract to a football club

# IAS 41 - Agriculture

## Scope of IAS 41



# Fair value

---

Fair value is defined as ...

... the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (IFRS 13p9).

There is a fair value hierarchy:

- Level 1 - Quoted price in active market
- Level 2 - No active market, but observable data: e.g. Recent market transaction prices; Market prices for similar assets; Sector benchmarks
- Level 3 – Unobservable inputs: e.g. Present value of expected cash flows

# Fair value of bearer plants

## Present value of expected cash flows - issues

- Need to make assumptions re yields, commodity prices, exchange rates, inflation rates, etc – maybe over 25 plus years
- For bearer assets, may have to start with inflows from processed output, not at point of harvest
  - Need to allow for profit margin on processing costs (as though a third party was doing the processing)
- Cash flows should be those of a market participant
  - If actual cash flows are used as the basis, valuation may include goodwill and other intangibles
- Present value likely to represent value of land as well as biological assets
  - Must eliminate - either by deducting value of land from present value, or including notional rent as a cash outflow

# Fair value of bearer plants

---

## Present value of expected cash flows - issues

To apply the DCF method successfully, you need to overcome these common difficulties:

- Inconsistent treatment of inflation in cash flows and discount rates
- What is the discount rate a market participant would expect?
- Dealing with the “...it’s just too difficult to predict (prices/exchange rates/interest rates)...” syndrome
- Not allowing long term projections to be unreasonably affected by short term fluctuations

# Fair value of growing produce

---

## Practical difficulties

In many cases it will be impractical to measure quantities:

- How many avocados on an avocado tree?
- How many (pickable) leaves on a tea bush?
- How many buds on a rose bush?
- How much sap in a rubber tree?

# Fair value of growing produce

---

## Practical difficulties

In some cases there is not an active market in agricultural produce at the point of harvest (e.g. sisal leaves)

In most cases there will not be an active market in immature growing produce (e.g. a half grown avocado)

When does produce start growing (e.g. blossom or bud?)

# Fair value of growing produce

---

## Possible approach - 1

1. Estimate time by which all produce growing at the reporting date will have been harvested
2. Estimate fair value of harvested produce over that period
3. Estimate cash flows required to bring that produce to harvest (including notional land rent)
4. Discount back to reporting date

# Fair value of growing produce

---

## Possible approach - 2

1. Estimate time by which all produce growing at the reporting date will have been harvested
2. Estimate fair value of harvested produce over that period
3. Assume that on average the produce is 50% mature
4. Fair value of growing produce = 50% of fair value of subsequent harvested produce

**OR**

- Conclude that measurement of fair value is clearly unreliable and measure at cost (on initial recognition of the growing produce)

# Cost model for bearer plants

---

## Measurement of cost

- Capitalise “costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management”
- IASB declined to include guidance on when this point might be reached, but recognized that there might already be growing produce on the plant at this point (probably right – leave it to management to take a sensible approach).

# Cost model for bearer plants

---

## Example – sugar cane

New cane takes about 18 months before harvest. The cane is then harvested as agricultural produce, leaving a stump known as a ratoon, from which two more crops are produced.

- At what point is the plant capable of operating in the manner intended by management? At the point the cane begins to grow or at the point the cane is ready for harvest?
- How does one determine the cost of the ratoon after the first harvest?

# Questions and answers?



THANK YOU