

A fair time for agriculture?

Are British farmers ready for IAS 41? Is anybody?
Julie Butler

IAS 41, *Agriculture*, requires biological assets to be measured at their fair value less estimated point-of-sale costs, except where fair value cannot be measured reliably. Its main provisions were described in Rieko Yanou's article in the April issue of *Accountancy* (pp 102-103). It does not deal with the processing of agricultural produce after harvest.

IAS 41 was published in December 2000 and applies for accounting periods beginning on or after 1 January 2003. In the absence of a relevant UK standard, IAS 41's provisions are not mandatory in the UK, but earlier adoption is 'encouraged' by the IASC – and, technically, even appears to be allowed by the provisions of existing UK company law.

However, the ICAEW has recommended that, for reasons of comparability, UK companies should not be allowed to comply with IASs before they are fully incorporated into UK requirements. Before a relevant standard is introduced in the UK, there will have to be the usual processes of consultation and exposure. At the time of writing, there has been no official response to IAS 41 from the UK Accounting Standards Board.

IAS 41 raises a number of interesting questions for the agricultural industry. It has been in such crisis recently that the introduction of what could be a very major change for agriculture has to date received little publicity in the farming press. The key issues include taxation. IAS 41 appears to be in direct contravention of the UK's tax guidance on farming stock valuation, BEN19 Inspectors Manual IM229, which states that the inspector of taxes is looking for a figure (commonly referred to as a valuation) that represents the stock's cost or, if lower, its net realisable value.

When looking at IAS 41's full impact on UK accounting procedures, it must be borne in mind that under current accounting principles it is normal to use the historical cost convention. So the current UK basis for valuing growing and harvested crops is the actual cost of production. It can prove difficult, however, to calculate actual costs, particularly feed costs for livestock, and in this instance 'deemed cost' is



acceptable. Deemed cost should be used when it is not possible to obtain actual costs from the records. It is the use of deemed cost that prepares the industry for fair value, because it involves arriving at a reasonable estimate of cost by taking a specific percentage of open market value. BEN19 gives the following rules for arriving at deemed cost:

	% of open market value
Cattle	65%
Sheep and pigs	75%
Harvested crops	75%

If an agricultural enterprise is using a significant amount of deemed cost calculations, it is easy to see the impact of changing to fair value and accounting for unrealised profit. So it could be argued that large parts of the industry are already prepared for IAS 41.

The 'herd basis', as we now understand it, would apparently have to go, at least for accounting purposes. The herd basis treats animals kept for production (or reproduction) as fixed capital. But IAS 41 applies to fixed capital as much as to stocks, so herds would have to be revalued regularly. As the use of current values for 'fixed assets' is allowed by FRS 15, *Tangible Fixed Assets*, there should be no need to amend existing standards in order to accommodate this. However, perhaps some adjustment to the accounting figures through the tax computation, which will effectively preserve the herd basis for tax purposes, will be allowed?

It is unclear how the new standard will impact on tax computa-

tions. Taxable profits are increasing, reflecting accounting profits under UK GAAP. Revenue practice is to accept any method the accountancy profession recognises, as long as it doesn't violate the taxing statutes as interpreted by the courts. If the ASB were to adopt IAS 41, then it is assumed that it would supersede BEN19, unless a rule of law supervened. This would have the disadvantage to the industry of increasing taxable profits and reducing taxable losses. Is the agricultural industry prepared for this?

There could also be concerns that fair value might give a misleading picture of the financial position in view of the UK weather and livestock problems – BSE and so on. Recent events demonstrate the problems of using fair values – soon after IAS 41 was published there were no UK markets for many biological assets, especially livestock, because of the foot-and-mouth crisis. This highlights what problems there could have been in recognising unrealised profits before the outbreak, or indeed during it.

As noted above, IAS 41 states that earlier application is encouraged, and existing UK standards already allow for 'fixed assets' to be shown at current values. But what about stocks? In theory, current values for stocks could be included in accounts, using the alternative accounting rules in the Companies Act. However, as we have already noted, the ICAEW has come out against early implementation of IASs, so businesses should await further direction. We assume that this will involve a lot of deliberation, debate and liaison, not least with the Inland Revenue.

These are certainly interesting times. Floods, plagues, pestilence and a change in the basis of measuring biological assets – look out for a rush for headache tablets!

At the time of writing, the ICAEW's Farming Group is considering the impact of IAS 41. This article is not intended to prejudge the group's conclusions.