ASPECTS REGARDING THE INTERNATIONAL ACCOUNTING STANDARD I.A.S. 41 - AGRICULTURE

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Abstract

At the end of the year 2000, the European Parliament passed a standard specifically addressing agriculture, the International Accounting Standard IAS 41 – Agriculture. This standard introduced the fair value evaluation model to agriculture. Based on this, one can approach the management of transforming biological assets, so that on the occasion of initial and final accounting of each economic exercise these assets can be evaluated at their fair value, diminished with the estimated selling expenses. According to this international standard, the agricultural activity represents "the management of biological transformations and harvesting biological assets, with the purpose of selling them or transforming them into agricultural products or supplementary biological assets". As Barry J. Epstein and Eva K. Jermakowicz note, "in the context of old international accounting standards, most of the rules applicable to agriculture (IAS 2 regarding stocks, IAS 16 regarding property and IAS 18 regarding income) deliberately excluded all or almost all examples related to agriculture. An analysis of financial statements issued for agricultural companies would have revealed the consequences of this neglect: a large array of methods and principles were applied by companies in the field of forestry or grain production. The objective of this standard is to prescribe the accounting treatment and information disclosure of agricultural activities". IAS 41 has to be applied "in the accounting of biological assets and agricultural products at the time of harvest and government grants. The Internation Accounting Standard IAS 41 becomes the starting point in the evaluation of the fair value of assets in the field of agriculture. The objective of the present paper is to present the main aspects of IAS 41 in Romania.

Key words: international accounting standards, agricultural accounting, biological assets, fair value, financial statements

A characteristic trait of agriculture is the fact that a part of the means of production is obtained directly from the production process.

This leads to a series of particularities connected to the acknowledgement and evaluation of the accounting structures characteristic to agricultural activities.

The specificity of agricultural activities determines a series of particularities at the level of financial accounting as well, on the one hand, from the point of view of assets and results, and on the other hand, from the point of view of specific documents.

Most of the business organizations involved in agricultural activities are relatively small, independent, usually associations or family enterprises, oriented towards cash accounting, often perceived as not obligated to present general financial statements.

Moreover, an international tendency towards liberalization, an increasing number of the societies internationally marketable, as well as a larger volume of investments, had an effect of increasing the dimension, area of applicability and commercial character of agricultural activity.

This has determined an even greater necessity for financial statements based on coherent accounting principles, universally accepted – the International Financial Report Standards (IFRS).

MATERIAL AND METHOD

Our approach has the objective of analyzing the IAS 41 standard.

Our research is focused on synthesizing the notions comprised by the specialty literature regarding the implementation of the IAS 41 standard. In order to reach this objective we have used a fundamental research methodology.

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RESULTS AND DISCUSSIONS

At the beginning of the year 2003, the international specialists in the design of norms reached the conclusions that agriculture cannot be excluded anymore from the area of applicability of IFRS; as a result, IAS 41 Agriculture was issued.

The objective of this standard is to prescribe "the accounting treatment and information presentations regarding agricultural activity".

IAS 41 establishes a set of criteria for agricultural activities, referring to the common characteristics amidst the diversity of the activities in agriculture:

–Animals and plants are capable of biological transformations;

–Management of transformation. The manner of management facilitates the biological transformation, or at least stabilizes the conditions which are adequate for the respective processes (for example, the level of nutritious elements, humidity, temperature, fertility and light). This system of management differentiates agricultural activity from other kinds of activities. For example, harvesting the products from resources that have not been managed (from example, oceanic fishing or deforestation) does not represent an agricultural activity;

–The evaluation of the transformation. The qualitative modification (for example, genetic quality, density, degree of maturation/ ripeness, protein content, degree of fibre resistance) or quantitative modification (for example, number of chickens, weight, volume, length or fibre diameter, number of ducklings), determined by biological transformation, is evaluated and monitored as a routine management function.

The Agriculture Standard is applicable in the accounting of biological assets, agricultural products at the moment of harvest and government subsidies.

IAS 41 Agriculture is neither applicable in the case of direct exploitation activities, nor for the agricultural product which is harvested and is, consequently, a non-biologic product.

Moreover, the standard does not refer to the accounting of agricultural production which is not included in processing.

Agricultural activity represents the management of biological transformations in plants and animals, therefore the management of biological assets for sale, as agricultural products or as additional agricultural products.

Biological assets represent the fundamental assets of agricultural activities, owned for their capacity for transformation. Barry J. Epstein and Eva K. Jermakowicz mention that biological assets are involved in two types of production: the first has to do with the modification of the assets, through maturation or breeding. The second one deals with making separable products, which can be regarded, initially, as agricultural production.

Biological assets are, most commonly, managed in groups (herds of animals, crop fields or clusters of trees).

In order to be able to talk about a group, its components have to be homogenous in nature, and homogeneity has to exist in the activity for which the group is used, as well.

For example, cherry trees which are used for fruit production will not be in the same group with those from which the wood is used.

Biological transformation entails the processes of growth, maturation and reproduction, which cause quantitative and qualitative modifications for a certain biological asset.

The harvest represents the separation of agricultural products or the termination of vital processes of a biological asset.

Biological assets are actually plants and live animals.

Biological assets are not identical with crops or agricultural production that is why the distinction between the former and the latter category is important, taking into account the fact that the accounting for each one could be different.

Acknowledging biological assets as such happens when:

–the entity controls the asset as a result of anterior events;

–there is a probability for economic benefits associated with the assets to enter the enterprise;

–the fair value or cost of the asset can be realistically evaluated.

The initial acknowledgement is done at acquisition cost or production cost, according to case, and for the balance is done as minus cumulated amortization and the cumulated provisions for depreciation.

Biological assets acknowledged as current assets are comprised by the category of stocks. It is to be noted that in this category fall young animals and animals of any kind (calves, lambs, piglets, foals and others) raised and used for reproduction, animals and birds that are fattened in order to be capitalized on, colonies of bees, as well as production animals – wool, milk, fur.

In what concerns cereal cultures, they are treated, from the viewpoint of accounting, as products on the stocks along their circle of production, while crops are regarded as finite products.

Stocks are evaluated using the model of historical cost. According to this model, assets are

initially acknowledged at cost value, and in the balance they are presented at the minimum between cost and the value that can be obtained by selling or using them.

After the initial accounting process, and at the closure of each financial exercise, biological assets have to be evaluated at their fair value, diminished with the estimated sale costs.

IAS 41 introduces in agricultural accounting the evaluation model based on fair value, from which the estimated costs of the sale point are subtracted.

This represents a major shift in comparison with the traditional model for evaluation, based on historical cost, applied on a large scale in the primary sector.

The evaluation based on fair value allows finding relevant information, reflecting the effects of modifications caused by the biological transformation of biological assets.

In determining fair value, the standard sets a hierarchy of approaches.

First of all, fair value corresponds to the price practiced on an active market.

An active market is a market where the following conditions are being fulfilled: the goods marketed are homogeneous; information buyers and sellers exist at any moment; prices are available to the public.

The modifications of fair value in biological assets influence directly the perspectives of regeneration of future benefits foreseen by the economic entity.

This type of evaluation influences the agricultural activities in which biological assets that generate future benefits have an economic life-cycle which exceeds the period of the financial exercise.

Using fair value as model for acknowledgement and measurement of biological increase leads to evaluating and reporting the income along the entire period of growth of a plantation, up until the moment of harvest.

Standard 41 Agriculture asks for the agricultural enterprise to use an approach based on fair value when it evaluates biological assets used in the agricultural activity, an exception being the cases when fair value cannot be coherently evaluated.

This exception from the model of historical cost is the most important aspects regarding this standard and creates an accounting model which corresponds to certain demands for accurate presentation.

Maybe it is for this reason that this new characteristic of IAS 41 has generated numerous debates at the stage of design and exposure.

Although the experts had in mind more evaluation modalities (net potential earnings, current cost or market value, as alternatives to historical cost), they finally reached the conclusion that fair value is the one that reflects most accurately the profits in the field of agriculture.

Supporters of this model bring arguments in favour of the idea that the effects of the modifications caused by biological transformation are best reflected through a reference to the modification of fair value for biological assets.

They consider that the modifications of fair value in the case of biological assets bear a direct connection to modifications appeared in the potential for future economic benefits to be generated by the enterprise.

The evaluation of agricultural activity based on fair value can be supported by a series of arguments:

–the evaluation of the cost of biological assets is sometimes less credible than the evaluation of fair value, because the coupled products and the coupled costs can create situations in which the relationship between entries and costs is incorrectly defined, leading to arbitrary calculations of costs in the case of various results of biological transformation;

–many biological assets are marketed with clear prices, and their presence strengthens significantly the credibility of market value as indicator of fair value;

–the continuous and relatively long production cycles, with episodes of instability in production as well as in the market environment, often lead to a lack of accord between the accounting period and a complete production cycle. In the absence of accounting related to fair value, the integral earnings from the long-term production process would be reported for periods that are too lengthy, which in turn would lead to a significant distortion of performance or of the financial status that corresponds to that period.

The transactions connected to the production of biological transformation possess a diminished connection to the biological transformation itself, and an even farther one with the expected economic benefits.

Nonetheless, IAS 41 allows for one exception from the fair value evaluation.

Thus, if at the moment of initial accounting of a biological asset there is no market price and the other evaluation methods of fair value are not applicable, the mentioned asset can be evaluated at acquisition cost, or at production cost diminished with whatever ulterior costs are necessary.

This exception, however, ceases to be applied if later on an adequate evaluation of fair value can be done.

Subsidies connected to biological assets evaluated at their fair value have to be included in accounting at the moment when all the conditions for receiving subsidies are fulfilled.

Even though the majority of studies are against the provisions of the IAS 41 standard for the evaluation of biological assets, there are supporters of this treatment as well.

Authors like Argilés and Slof underline the fact that the generalization of this model is beneficial for small family farms, which possess limited resources and limited abilities to calculate their costs.

Other authors, like Barlev and Haddad, state that fair value in accounting leads to divulging information in a complete manner and is compatible with transparency.

In other words, fair value involves simultaneously an evaluation method that is more consistent and an information source that is more adequate and can be more easily compared.

Another element of novelty of IAS 41 Agriculture is represented by the accounting of government subsidies related to agricultural assets.

IAS 41 modifies this treatment in the case of reporting by an entity of an unconditioned government subsidy, connected to biological assets evaluated at fair value minus estimated sale costs.

Thus, "an unconditioned government subsidy for a biological asset evaluated at fair value minus the costs generated by sale has to be acknowledged as profit or loss only and only when the government subsidy becomes eligible."

If a government subsidy offered for a biological asset evaluated at its fair value minus sale costs is conditioned, including here the case when a government subsidy forbids an entity from engaging in specific agricultural activities, an entity has to acknowledge the subsidy as profit or loss only when the conditions for the subsidy are satisfied.

CONCLUSIONS

Standard IAS 41 sets the accounting treatment for agricultural activity, presenting financial statements and information. The standard focuses primarily on the evaluation of biological assets based on fair value.

The implementation of the standard in various countries has led to a radical change of accounting practices for large agricultural societies, through the shift from evaluating in historical value to the evaluation in fair value.

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