

**THE POLITICAL PROCESSES AND ROLE OF GATEKEEPERS  
IN SETTING ACCOUNTING STANDARDS  
FOR AGRICULTURE**

**By**

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## ABSTRACT

Many accounting regulations are introduced in response to crises of some kind, arising from a corporate collapse or claims that published financial reports have been misleading. In contrast, the IASC's IAS 41 *Agriculture* standard was developed from the mid-1990s and issued in 2000, two years after the Australian AASB 1037 *Self-Generating and Regenerating Assets (SGARA)* standard, followed in 2004 by New Zealand's NZ IAS 41 *Agriculture*. There had been no prior crisis or public expression of concern about shortcomings in existing practice. This study considers the background to the emergence of accounting for agriculture onto the agenda of standard-setting bodies, and the role played by different insiders. Here, they are collectively termed 'gatekeepers', the key staff, expert technical advisers and decision-makers who were members of standard-setting boards.

Examination of the development of these new standards extends beyond consideration of technical accounting issues. Several case studies identify the regulatory and political processes each standard-setting agency adopted to consider and then progress the topic through all rule-making stages and resulting lobbying activities by significant users. These political processes are examined using the Cobb and Elder (1972, 1983) agenda-building framework and the Cobb, Ross and Ross (1976) analysis of institutional dynamics.

The history of accounting for agriculture, in Australia and New Zealand, is traversed to explain the historical background to the new omnibus agricultural standards promulgated in Australasia. Significant events described include the AASB staff recommendation to the IASB in 2003 to split IAS 41 in two before its designated 2005 commencement date – a recommendation which, so far, has been ignored.

New research material includes unpublished documents relating to the initial AASB *Project Brief* and IASC *Point Outline* background proposals for each standard, the IASC's Field Test Report prior to adopting its IAS 41 standard and the AASB 1037 standard post implementation review – possibly the first ever to be undertaken.

The study found that the activities of key insiders were consistent with what Cobb *et al.* (1976) described as the *inside access* model, both in placement of the topic on the agenda

and then subsequent incorporation of proposals for fair value accounting for agriculture. A feature of the events described in this study was the interaction between the different standard-setting bodies – a possibility little-described in the accounting literature, and arguably a significant element in the manner in which standards were considered and developed by the IASC, and latterly the IASB.

Overall, a combination of intra- and inter-agency lobbying resulted in compromise reflected in the final text of IAS 41. This modified the full fair value accounting proposal. The study found that gatekeepers paid little regard to submissions from experienced industry representatives, accountants, academics and other commentators world-wide. Practical evidence from parties concerning the utility of the proposed new rules was requested too late to influence the content of the final IAS 41 standard. Not surprisingly, the standard is still controversial.

**Key words:** AASB, AASB 1037, Agenda Building & Standard Setting, Agriculture, Gatekeepers, Fair Value Accounting, IASC, IAS 41, Lobbying, Post Implementation Review, SGARA.

## STATEMENT OF ORIGINALITY

This is to certify that to the best of my knowledge, the content of this thesis is my own work. This thesis has not been submitted for any degree or other purposes.

I certify that the intellectual content of this thesis is the product of my own work and that all the assistance received in preparing this thesis and sources have been acknowledged.

A handwritten signature in black ink, appearing to read 'J. H. Milne', with a stylized flourish at the end.

John Herbert Glanville MILNE

26th October, 2011



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The objectives of this thesis were to determine how accounting standards for Agriculture originated in the form they did and to understand reasons why. Initially there were two standards developed at about the same time by two different standard-setting bodies. Each was controversial from the start. Their study has led along paths and by-ways unfamiliar to my experience as a businessman, chartered accountant and professional director.

My fellow directors, professional accountants and auditors at Grove Mill Wine Company expressed initial unease. Mark Peters, Alton Jamieson, David Appleby, Jane Trought, Graeme Mitchell and Dan Williams urged me to find out more.

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Notwithstanding all the foregoing, any errors or omissions and all judgements, expressed or implied, are mine; so, solely my responsibility.

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## GLOSSARY OF ABBREVIATIONS

<b>AARF</b>	Australian Accounting Research Foundation	
<b>AAS</b>	Australian Accounting Standard	
<b>AASB</b>	Australian Accounting Standards Board	
<b>AASB 1037</b>	'SGARA' Standard	(Australia)
<b>AICPA</b>	American Institute of Certified Public Accountants	
<b>ACAG</b>	Australasian Council of Auditors-General	
<b>ACF</b>	Advocacy Coalition Framework	
<b>APB</b>	Accounting Principles Board	(U.S.A.)
<b>ARSB</b>	Accounting Research and Standards Board	(New Zealand)
<b>ASB/ASC</b>	Accounting Standards Board/Committee	(U.K.)
<b>ASEAN</b>	The Association of Southeast Asian Nations	
<b>ASRB</b>	Accounting Standards Review Board	(Australia)
<b>ASRB-NZ</b>	Accounting Standards Review Board	(New Zealand)
<b>ASX</b>	Australian Stock Exchange Limited	
<b>BA</b>	Biological Asset/s	(IASC)
<b>CAR</b>	Council of Annual Reporting	(The Netherlands)
<b>CICA</b>	The Canadian Institute of Chartered Accountants	
<b>CLERP</b>	Corporate Law Economic Reform Program	(Australia)
<b>CMV</b>	Current Market Value	
<b>CPA</b>	Australian Society of Certified Practising Accountants	
<b>CRC</b>	Compounded Replacement Cost	(FCL/FCF)
<b>DCF</b>	Discounted Cash Flow	
<b>DP 23</b>	Discussion Paper No. 23 – Accounting for <i>SGARAs</i>	(Australia)
<b>DSOP</b>	Draft Statement of Principles <i>Agriculture</i>	(IASC)
<b>E65</b>	Exposure Draft No. 65 <i>Agriculture</i>	(IASC)
<b>EC</b>	European Commission	
<b>ECSAFA</b>	Council of the Eastern, Central and Southern African Federation of Accountants	
<b>ED 83</b>	Exposure Draft No. 83 <i>SGARA</i>	(Australia)
<b>ED-90</b>	Exposure Draft No. 90 <i>Agriculture</i>	(New Zealand)
<b>ED 114</b>	Exposure Draft 114 <i>Agriculture</i>	(Australia)
<b>FASB</b>	Financial Accounting Standards Board	(U.S.A.)



<b>FCL/FCF</b>	Fletcher Challenge Ltd./Fletcher Challenge Forests	(New Zealand)
<b>FRA</b>	Financial Reporting Act, 1993	(New Zealand)
<b>FRC</b>	Financial Reporting Council	(Australia)
<b>FTP</b>	Field Test Project	(IASC)
<b>FRS</b>	Financial Reporting Standard	(U.K. & N.Z.)
<b>FRSB</b>	Financial Reporting Standards Board	(New Zealand)
<b>G4+1</b>	Standard setting bodies for Australia, Canada, New Zealand, the U.K. & U.S.A., with IASC representatives as observers	
<b>G-100</b>	Group of 100 Inc.	(Australia)
<b>GAAP</b>	Generally Accepted Accounting Practice	
<b>GPFR</b>	General Purpose Financial Report	
<b>HC</b>	Historical Cost	
<b>IAS</b>	International Accounting Standard	(issued by the IASC)
<b>IAS 41</b>	'Agriculture' Standard	(IASC)
<b>IASB</b>	International Accounting Standards Board	
<b>IASC</b>	International Accounting Standards Committee	
<b>ICAA</b>	The Institute of Chartered Accountants in Australia	
<b>ICAEW</b>	The Institute of Chartered Accountants of England and Wales	
<b>ICANZ</b>	The Institute of Chartered Accountants of New Zealand	
<b>IOSCO</b>	International Organisation of Securities Commissions	
<b>IFAC</b>	International Federation of Accountants	
<b>IFRIC</b>	International Financial Reporting Interpretations Committee	
<b>IFRS</b>	International Financial Reporting Standards	
<b>IPSAS</b>	International Public Sector Accounting Standards	(issued by IFAC)
<b>KDQ</b>	Key Decisions Questionnaire	(AARF)
<b>MV</b>	Market Value	
<b>NCV</b>	Net Current Value	
<b>NMP</b>	Net Market Price	
<b>NMV</b>	Net Market Value	
<b>NPV</b>	Net Present Value	
<b>NRV</b>	Net Realisable Value	
<b>NSW</b>	New South Wales	(Australia)
<b>NZFP</b>	New Zealand Forest Products Limited	

<b>NZ-GAAP</b>	New Zealand Generally Accepted Accounting Practice	
<b>NZ-IFRS</b>	New Zealand International Financial Reporting Standards	
<b>NZSA</b>	The New Zealand Society of Accountants, Inc.	(New Zealand)
<b>NZWC</b>	The New Zealand Wine Company Limited	(New Zealand)
<b>PP&amp;E</b>	Property, Plant and Equipment	
<b>PER/PIR</b>	Post-Enactment (or Implementation) Review	
<b>PSASB</b>	Public Sector Accounting Standards Board of the AARF (Australia)	
<b>QDPI</b>	Queensland Department of Primary Industries	(Australia)
<b>RA</b>	Recoverable Amount	
<b>RIRDC</b>	Rural Industries Research Development Corporation	(Australia)
<b>SAC</b>	Statement of Accounting Concepts	(Australia)
<b>SAP</b>	Statement of Accounting Practice	(Australia)
<b>SC</b>	Steering Committee ‘Agriculture Project’	(IASC)
<b>SEC</b>	Securities and Exchange Commission	(U.S.A.)
<b>SGARA</b>	<i>Self-Generating and Regenerating Assets</i>	(Australia)
<b>SME</b>	Small and Medium-sized Entities	(IASB)
<b>SONOME</b>	Statement of Non-Operating Movements in Equity	(AARF)
<b>SSAP</b>	Statement of Standard Accounting Practice	(New Zealand)
<b>Tas.</b>	Tasmania	(Australia)
<b>Top-500</b>	ASX Top-500 Listed Entities	(Australia)
<b>TPA</b>	Technical Practice Aids	(New Zealand)
<b>TPA-5</b>	TPA No.5 – Accounting for Livestock	(New Zealand)
<b>TPA-7</b>	TPA Aid No.7 – Accounting for Bloodstock Enterprises (New Zealand)	
<b>UIG</b>	Urgent Issues Group	(Australia)
<b>U.K./UK</b>	United Kingdom	
<b>UNE</b>	University of New England	(Armidale, NSW)
<b>U.S.A./US</b>	United States of America	
<b>Vic.</b>	Victoria	(Australia)
<b>WA</b>	West Australia	(Australia)
<b>WP</b>	Working Paper	(UNE)

## Section 1. INTRODUCTION AND OVERVIEW

Accounting and financial reporting for agricultural entities entered the formal agendas of each of the Australian and International standard-setting bodies during the early 1990s. There was no external crisis or popular concern about misleading reporting by agricultural preparers. Instead separate proposals for new standards were sponsored by insiders within respective regulatory bodies. This study examines the role of those key staff, technical advisors and decision-makers who were also Board members, collectively the gatekeepers. It also examines the political and rule-making processes for each standard-setting body in developing these standards, and subsequent events in Australia and New Zealand.

The AASB 1037 *Self-Generating and Regenerating Assets (SGARA)* standard was developed in Australia during the mid-1990s by the Australian Accounting Research Foundation (AARF), and issued by the Australian Accounting Standards Board (AASB) in May 1998. During the mid- to late-1990s the International Accounting Standards Committee (IASC) in London was also undertaking its due processes for developing the IAS 41 *Agriculture* standard.<sup>1</sup> This was approved in December 2000. The standards were similar. Each finally proposed and adopted fair value measurement accounting principles for biological assets and their produce.

There was no common accounting practice for agriculture prior to issuing the new standards. ‘Best practice’ guidelines and accounting rules had been developed to reflect practical circumstances for most individual agricultural sectors, but not all. Development of the new standards was not confined solely to addressing technical accounting matters. Other processes were involved too. Respective standard-setting agencies followed virtually parallel consideration stages from disparate beginnings. Each evolved separately and contained important initial differences in scope and detail.

Once IAS 41 *Agriculture* was approved, it transferred as a new international standard in Australia in July 2004 for convergence as AASB 141; and in November 2004 to New

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<sup>1</sup> The convention adopted for the case study is that generic accounting standards refer to the International Accounting Standard. *e.g.* IAS 41 *Agriculture* or IAS 2 *Inventories*. However a local accounting standard is referenced where relevant, *e.g.* in Australia: AASB 1037 *Self-Generating and Regenerating Assets* – for which the *SGARA* abbreviation is also used.

Zealand, for harmonisation as the equivalent international financial reporting standard NZ IAS 41.

Young (1994) suggested: *'the addition of an accounting problem to the technical agenda...is a necessary condition for the subsequent issuance of accounting standards'* (p. 83). Development of two comparable accounting standards by two leading standard-setting bodies at about the same time might suggest a major accounting problem had arisen creating a specific need to issue a new standard.

There was no sign of any crisis due to accounting failure or misleading reporting by agricultural entities. Admittedly, historically, there were differing income reporting and inconsistent asset valuation bases adopted by listed agricultural companies, especially for forestry. This was because there were no approved accounting and reporting rules for this sector. Nor was there user demand for a new standard. When the new standards were being considered there was no reference to published research into users' requirements or to normative studies as to what agricultural entities 'should' report. Paradoxically, there was recognition of the need for consistency in accounting rules applied to agricultural activities.

The new standards created problematic accounting and reporting rules for various agricultural reporting entities. Problems included potential multiple reporting of revenues for the same income stream; advanced income recognition, potentially years before realisation; inflated inventory valuations compared to other industries and different recognition rules for reporting changes in asset valuations through the income statement.

As a result, AASB 1037 and IAS 41 were controversial. Determined lobbying continued from affected sector industry representatives, users and other accounting interests since these standards created accounting problems especially for bearer-agricultural entities, their auditors and investors, where none existed before. That persists to the present day. Standard setters have resisted consideration of these issues because of higher priorities elsewhere.

Placing these elements into context requires an analytical framework to examine the accounting rule-making processes and consequent lobbying activities.

Walker and Robinson (1993) described why these processes are incompletely understood:

- issues examined by researchers were limited to items already on a formal agenda;
- studies have examined only written submissions which provide limited insights into the nature of the political activity surrounding accounting rule development; and
- little attention has been directed to the questions:

How do issues gain admission to the agenda of a rule-making body?...What prompts the rule-making body to review or enact an accounting rule?, and Who are the gatekeepers that control the rule-making agenda? (p. 9).

Whilst Howieson (2009) repeated the question raised by earlier empirical studies of written submissions: *'Are standards setters responsive to concerns of lobbying entities and interest groups?'* (p. 578).

Using methodology described by Yin (2003), the research reported below addresses these questions over the decade from the mid-1990s with separate case studies for each of the AASB and IASC. It considers 'how' the new agriculture topics gained access to respective agendas and internal deliberations into formulating agriculture accounting principles, and 'what' prompted each rule-making body to develop the *SGARA* and *Agriculture* accounting rules in their standard-setting domains - including subsequently in Australia and New Zealand. It describes 'who' the gatekeepers were controlling respective rule-making agendas. Finally, the study considers 'how' respondents expressed concerns about the proposals progressively, and the responsiveness of the gatekeepers.

The analytical framework selected was the model initially outlined by Cobb and Elder (1972) as summarised by Walker and Robinson (1993). This model describes 'how' a topic progresses through rule-making regulatory agendas. An advantage of the Walker and Robinson summary was reference to a final post-enactment review (PER) stage.<sup>2</sup>

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<sup>2</sup> The generic term adopted is a post-enactment review (PER). Inclusion of this stage in Walker and Robinson (1993) may have reflected prior Australian experience. Legislation establishing Australia's former Accounting Standards Review Board (ASRB) required auditors to report instances of non-compliance with approved standards to the ASRB – apparently with the aim of assisting post implementation reviews. In May 2003, the AASB conducted a post implementation review (PIR) for the AASB 1037 *SGARA* standard.

Accounting concepts also changed through time on relevant reporting principles for an omnibus agriculture standard. External support for these proposals was sought from the standard-setting constituencies. However there was selective use and general lack of responsiveness to submissions by both AASB and IASC standard-setting agencies. Rather, the standards that were developed appeared to reflect the views of ‘insiders’, consistent with the Cobb, Ross and Ross (1976) *inside access* model. There was also lack of transparency in formal reporting by standard setters on the results of their surveys seeking to gauge acceptability of the new standards from users.

Finally, this ‘Accounting for Agriculture’ study provides a comprehensive commentary on how the Australian and IASC rule-making processes operated in practice and how they interacted. The concurrent evolution of two similar standards, virtually in parallel, within two domains has been little examined before together with the interaction of two standard-setting agencies and associated inter-agency lobbying to influence a desired outcome. Exceptions include the discussion of interaction between Australian government agencies and a standard-setting agency described by Walker (1992), conflict between Australian public- and private-sector agencies (Walker and Robinson, 1994), and similar interactions between the FASB and the U.S.A.’s SEC (examples cited in Walker and Robinson, 1993).

The outcome was a combination of intra- and inter-agency lobbying resulting in compromise in the final text of IAS 41. This modified the full fair value accounting proposal. The study found that gatekeepers paid little regard to submissions from experienced industry representatives, accountants, academics and other commentators world-wide. Practical evidence from parties concerning the utility of the proposed new rules was requested too late to influence the content of the final IAS 41 standard. Not surprisingly, the standard is still controversial.

The study is organised as follows:

Section 2 examines the evolution of agenda-building political process dynamics; the role of the gatekeepers and lobbying literature; application to accounting standard setting and the rationale for employing case studies; the research questions and design, together with an overview of the topic of accounting for agriculture;

Section 3 reviews historical technical guidelines, particularly in Australasia, and agricultural sector accounting practice prior to, and as background for, the reasons behind development of the new standards;

Section 4 discusses the sequential rule-making processes from 1995 to 2000, from issue access to promulgation of the new standards by the AASB and the IASC respectively, the activities of their key internal and technical staff; and external and inter-agency lobbying at relevant rule-making stages;

Section 5 describes transfer of the IASC's IAS 41 *Agriculture* standard to Australia and New Zealand. By then there was ample adverse comment from academics and others about the standards, together with practical experience from preparers reporting under the Australian standard. The IASB had no desire to amend IAS 41 before the 2005 commencement date. Implementation issues were therefore referred to the International Financial Reporting Interpretations Committee (IFRIC) to seek interpretations or amendments to rectify original oversights and error in the IAS 41 standard;

Section 6 discusses the AASB's post implementation review of its AASB 1037 *SGARA* standard after two years practical experience. This PIR was a first. The aim was to propose recommendations to the IASB for improvements to IAS 41 before the operative 1 January 2005 implementation date. The principal recommendation to the IASB arising from this PIR was to split the standard in two. This was ignored;

Section 7 concludes with, a summary of major findings, areas for possible future research, observations about the case study and a process recommendation arising from the issue of the *Agriculture* international accounting standard;

The Appendices contain, *inter alia*, full documentation, not published before, about the initial bases for development of the two standards, the IASC's Field Test report on the proposed IAS 41 standard and the AASB's recommendations to the IASB from its post implementation review on the AASB 1037 standard, together with the full PIR report.

## Section 2. LITERATURE REVIEW AND USE OF CASE STUDIES

### Introduction

The role of the accounting standard-setter ‘gatekeepers’ has been recognised as an under-investigated area of interest requiring closer study (Walker and Robinson, 1993; Howieson, 2009). Gatekeepers include board members responsible formally for deciding upon and issuing standards. Here, the focus is also on those key staff and other technical advisers who supported standard-setter Boards.

The gatekeepers’ role is examined in course of reviewing the processes used to establish Australia’s AASB 1037 *Self-Generating and Regenerating Assets (SGARA)* standard issued in 1998, followed separately by the IASC’s IAS 41 *Agriculture* standard issued in 2000.

This section reviews the general literature relating to rule-making processes and lobbying activities relevant to the development of regulations, before delving into the specific role of the gatekeepers and key insider staff in the development of accounting standards.

External lobbying processes and lobbyists’ strategies surrounding issue of the new agriculture standards are examined. Evidence is also supplied about the complexity of inter-agency lobbying occurring within and between national standard-setting bodies and country delegation representatives serving as voting, representational or technical delegates within the IASC Board structure.

The section provides reasons for undertaking several case studies to examine the agenda-building and rule-making analytical framework. These identify the political processes followed and the key roles of gatekeepers, and inherent compromises, in the establishment of the *SGARA/Agriculture* accounting standards, including the sources of evidence used in the study.



## Chapter 1. THE ROLE OF GATEKEEPERS AND ACCOUNTING STANDARD-SETTING PROCESSES

### 1.1 Gatekeepers and their Role in Development of Regulatory Activities

The establishment of rules for accounting and presentation of financial statements, and more generally, issuing approved accounting standards is a form of regulation. The literature on agenda building and regulatory processes, notably the contributions of Cobb and Elder (1972, 1983), Mitnick (1980), Kingdon (1995) and Majone (2006), provides a framework to consider how, and when, issues are considered by rule makers, the processes followed, and the manner some parties manage or control the formal agenda.

A brief examination of the general regulatory and political process framework follows before considering its application to accounting standard setting.

Cobb and Elder (1972) refer to the systems research work of Easton (1965) to identify the political nature and processes in agenda-building. Easton sought to explain how wants, or demands, became inputs into a political system calling for political action. Demands cannot always be accommodated. They must first be converted into an issue fit for consideration as an agenda item by an authoritative decision maker:

Easton calls the process by which demands and issues enter or fail to enter the political system or any of its subsystems “gatekeeping”. Those persons, institutions, and groups whose actions determine the success or failure of a demand or issue entering into the system or any of its subsystems are termed “gatekeepers” (Cobb and Elder, 1983, p. 19).

Gatekeepers’ decisions determine whether an issue is accepted into the political process: *‘thus gatekeepers are key participants in the continuous process of agenda-building’*. The gatekeepers, who could include members of the regulatory agency or key staff, influence the passage of an issue through the political agenda - not only at point of entry, but also to monitor the load on the regulatory body’s formal agenda by selective consideration, or restriction of *‘its inputs and withinputs’* (*ibid.*, p. 19).

In this context, the ‘agenda’ is the scheduling of specific issues or topics for consideration by the decision-making body. These processes identify the discrete phases

shaping the full career of a political issue promoted by the gatekeepers. Cobb and Elder (1983) described the various stages as:

- agenda access, being issue creation, issue expansion and agenda entrance. This reflects the initial processes of the regulatory body in defining and initiating an issue, then adding that issue onto its agenda as a topic for consideration; followed by
- maintenance of the topic as an agenda item until formal agenda consideration, decision and promulgation, or its denial; and then to
- assess the impacts of the decision, that is, any subsequent review; until, eventually, the issue is terminated – unless later revived through another agenda-entrance process.

These political processes produce a form of regulation imposed by the regulatory body on others. Regulation itself may be defined as *'the intentional restriction of a subject's choice of activity, by an entity not directly party to or involved in that activity'* (Mitnick, 1980, p. 20). It envisages a regulator responsible for the regulated activity. Members of the regulatory body conduct these activities. The 'gatekeepers' include the formal regulatory decision-makers, staff advisers and contractors (Mitnick, 1980), who are able to define, initiate and develop issues to meet institutional agendas (Kingdon, 1995; Majone, 2006).

Collectively the gatekeepers govern the way an item enters the agenda and then controls consideration within the regulatory institution. These processes may be facilitated by 'brokers', to chaperone an issue through the maze of internal processes, 'access initiators', who build support for an issue as it progresses, or 'policy entrepreneurs' who act as prime movers *'in promoting policy innovation'* (Cobb and Elder, 1983, p. 187).

Oh (2004) and Coffee (2006) describe the ways in which the term 'gatekeepers', and the 'gate-keeping role', has wider applications and connotations across many disciplines. However, none of these adequately describe the political process phases outlined above.

Mitnick (1980) traced the life cycle of regulatory agencies and gatekeepers' roles.

The gatekeepers comprise more than the formal decision-making board. They were described more comprehensively as the regulator-bureaucrat archetypes identified

respectively, depending on their self-selected role, or combination of roles, as climbers, conservers, advocates, loyalists, zealots or statesmen.<sup>3</sup>

Downs (1957) postulated that in the development phase of a regulatory agency the group is likely initially to be headed by ‘a leader’, a statesman, and the gatekeepers, including insiders, are likely to be advocates, climbers or zealots who must seek external support, and recognition, to survive (p. 51).

Members of a regulatory body may operate in a full- or part-time governance capacity. Even though the chairman may have the highest statesman-like profile, s/he is not necessarily fully involved with each proposal or issue being considered. Collectively, board members are unlikely to read all submissions made on a topic, unless as a chairman or on a specific working group. Instead, ‘*board members may only read the summary or recommendations of staff*’ (Mitnick, 1980, p. 68).

This emphasises the importance of key internal staff involved in preparing support papers for formal board agendas; including the conceptual, technical and economic nature of arguments advanced by internal and external interested parties (Walker and Robinson, 1993; Hodges and Mellett, 2004). However, a designated voting majority of board members in their ultimate gatekeeping capacity are the formal decision-makers.

Individual gatekeepers may be appointed as representatives of constituencies, delegations or for their technical expertise. They have virtually sole discretion within a legislative or reputational mandate, not necessarily subject to public gaze or responsive to public need.

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<sup>3</sup> *Climbers* may be expected to seek expansion in regulatory agency size and mandate and to push for ever-more-complex regulations...and [thus] provide excuse for more workers and so more [regulatory] status; *Conservers* seek to retain their existing rewards...generally oppose expansion of the agency and its mandate because of the threat to the existing incentive system...the agency [may seek to maintain] stability in its environment in its own interest; *Advocates* seek to protect the agency’s goals and functions. If through expansion a threat to survival of the agency’s programs is co-opted or removed, they will back it...but if it fragments decision and potentially interferes with achievement of organisational or program goals they might [back it] if they believed increased specialization or professionalization might aid the agency in some way; *Loyalists* will be agents for some individual and may act as he wishes, assuming their self-interest permits. Behaviour depends on which of the previous three archetypes he represents; *Zealots* will push for achievement of their narrowly conceived programs. [They] will generally oppose industry influences threatening [their] project...[and] will favour [its] maintenance or expansion; and *Statesmen* will do what they think is best for society...[with no indicated] predictions regarding maintenance or expansion Mitnick, (1980, pp. 166-8).

The board, and key staff members, can wield significant power given '*they hold exclusive power over their agenda...(such that) a monopoly agenda setter can achieve almost any desired result*' (Majone, 2006, p. 229). This is reinforced by presumptive rights by virtue of experience or understanding of particular types of problems as the source of legitimacy to participate in the agenda-building process (Cobb and Elder, 1983, p. 184). Technical problems may be regarded as matters best delegated to experts. Kingdon (1995) also identified the policy stream of ideas generated by specialists. Mitnick (1980) considered the issue of representative decision-making vs. expert trusteeship: '*the trustee is technically expert on regulatory matters and assumes that whatever preferences guide his decision can easily be known...and the people they represent know what's to their own good*' (p. 325). That may help insulate and preserve prevailing bias in policy setting to maintain exclusive control over the board's decision-making area of responsibility.

Key staff may chair or conduct committee deliberations and also contract working groups, task forces or consultants to investigate specific topics. Their views can help mould or shape an issue. They can exercise a powerful support role for the Board. Their actions can also guide processes through the formal agenda. They have privileged power to control the progress of a topic, its form and content, and can influence deliberations upon a topic's entrance, priority and continued status as an agenda item.

Thus this agenda process provides '*a framework for integrating existing knowledge and guiding future research*' (Cobb and Elder, 1983, p. 169). Consideration of any regulatory process should consider the '*life cycle of an activity from issue access, the creation of a regulatory issue and its transformation into a policy intention*' (Mitnick, 1980, p. 81). Typical intermediary stages include issue access through some external or internal '*trigger device*' (*ibid.*, 1983, p. 85); then issue-expansion to mobilise support amongst decision makers, and key staff gatekeepers, to progress a topic onto the regulatory agenda; and thence to final decision including promulgation, subsequent review and/or formal termination off the agenda (*ibid.*, 1980, p. 169).

An alternative longer-term perspective was provided by Sabatier and Jenkins-Smith (1993). They preferred an Advocacy Coalition Framework (ACF) approach to policy development analysis compared to the more discrete '*heuristic stages research*' framework

described above. The ACF approach has merit. It identifies the potential for policy-oriented learning available from experience leading eventually to policy change. This might occur, for example, following practical experience or from a formal review process were that to happen as a final agenda stage. Critical to the ACF approach is willingness by gatekeepers to learn from that experience, and act upon those results.

The general regulatory and agenda political process analysis described above is directly applicable to the development of accounting standards by local and international standard setters. The standard setter is the regulator, responsible for the regulated activity of setting accounting standards, supported by key insider staff and technical advisers. Board decision-making processes and decisions to establish accounting standards, amendments or guidelines have widespread effects. Those regulated are the users of the standards and, more importantly, the resulting formal financial reports, including preparers, professional accountants, auditors, shareholders, investors, analysts, creditors and other stakeholders.

The political processes establishing accounting standards – as a form of regulation – have been examined by several commentators over three decades (*e.g.* Moonitz, 1974; Hope and Gray, 1982; Fogarty *et al.*, 1992; Walker and Robinson, 1993; Young, 1994; Kingdon, 1995; Stoddart, 2000; Hodges and Mellett, 2004; Jones *et al.*, 2004). They outline the activities involved, or explain the outcomes. However many of these studies describe a *'late and relatively insignificant phase of the political processes surrounding rule-development in accounting'* (Walker and Robinson, 1993, p. 5), rather than the early agenda access and entrance stages. Gatekeepers are likely to be critical to these stages. *'Again, studies that only examine responses to certain issues may be disregarding more interesting questions about why and how these issues were identified and what came of them following the release of the accounting rule'* (p. 10).

This study therefore focuses on each of the early agenda access and entrance stages, the rule-making processes and then what occurred after release of the *Agriculture* standards in the international and national Australian and New Zealand domains.

Beresford (1988), as a former Chairman, provided insight into the criteria the Financial Accounting Standards Board (FASB) used to decide whether to add a project to its agenda:

the Board considers four criteria: pervasiveness of the problem, availability of alternative solutions, technical feasibility, and practical consequences [given] the Board accepts its designated role as the independent standards-setting organization charged with the responsibility of improving financial reporting ... [and then] how we strive to make sure the FASB is working on the right issues, how we weigh input from our constituents, and how we endeavor (*sic*) to reach answers' (1988, pp. 1-2).

Later, Beresford (1993) repeated the above, and in addition further described the Board's '*balancing act*' to ensure all preparatory internal work processes were sufficient and completed before prioritising potential accounting-standard projects so that the Board and staff were all working in concert. Thus the Board and staff gatekeepers identify as a process how the problems they confront will be addressed (Cobb and Elder, 1983, p. 152).

The Cobb and Elder agenda-building concepts were summarised by Walker and Robinson (1993) to provide a framework for studying profession-sponsored rule-making processes and associated lobbying activities. This stages-based model provides a logical progression from one chronological phase to the next:

***Table 1. Elements of the Profession-Sponsored Rule-Making Process***

<b>Rule-Making Stage</b>	<b>Elements</b>	<b>Modes of Lobbying</b>	<b>Evidence</b>
<b>A. Agenda Entrance</b>	1. Issue emerges and gains admission to agenda	Discussions with members of regulatory bodies, politicians, <i>etc.</i> ; pressure through media reports, campaigns	Surveys, government reports; newspaper and other media comment
<b>B. Formal Consideration of Agenda Items</b>	2. Discussion memorandum or paper drafted and released	Written submissions, informal discussion	Written submissions
	3. Exposure draft(s) prepared and released	Written submissions, informal discussions	Written submissions media releases
	4. Open hearings and working parties	Representations to regulatory body	Transcripts of testimony
	5. Standard prepared, approved and issued	Press releases; meetings of professional bodies; contact with regulators and politicians	Text of standards/policy notes
<b>C. Post-enactment Review (PER)</b>	6. Assessment of impact of approved standard	Press releases; meetings with various professional and government bodies; non-compliance with accounting standards	Review letters; reporting practices

Source: Walker and Robinson (1993) Table 1, p. 7.

Analysis of the processes surrounding consideration of the U.K. ASB Application Note to FRS-5<sup>4</sup> caused Hodges and Mellett (2004) to invert the above Table. They sought to illustrate that at the ‘agenda entrance’ stage, at the foot of their table, lobbying activities ‘*may well up into the public domain once they have coalesced and gained sufficient support to influence the regulatory outcome*’ (p. 21). Further columns were added to their table to reflect informal lobbying and formal evidential processes.

Both frameworks provide an ‘*analytic distinction...between visible and hidden participants*’ (Majone, 2006, p. 238) or ‘*visible and hidden clusters*’ (Kingdon, 1995) and each envisages a positive issue creation, agenda entrance, consideration and promulgation process; and ideally, a review process.

In principle, the accounting standard-setter’s gatekeeper role extends beyond simply considering new or revised accounting standards. There is a further responsibility as ‘*an actor monitoring the quality of information, products and services*’ (Oh, 2004, p. 735) to interpret unforeseen issues arising out of a new standard. These should be identified beforehand through the formal exposure draft agenda consideration stage, presuming lobbyist’s concerns were recognised, and, where relevant, through an experimental or actual research programme. Afterwards, determination of the ‘*flaws and defects*’ (Coffee Jr., 2006) may occur through a formal post-enactment review process to ensure a new standard is meeting intended requirements (Walker and Robinson, 1993).

Each Table 1 Rule-Making Stage is relevant for this study into the role of the gatekeepers and the associated internal and external political processes leading to initial consideration, issue and review of the new *Agriculture* standards. However the agenda-building literature does not address the gatekeepers’ post-enactment review responsibility, and when this might occur. Possibly because it is rarely considered or undertaken, let alone reported – or, how resultant policy change and learning may best be achieved (Sabatier and Jenkins-Smith, 1993).

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<sup>4</sup> The Application Note was a proposal by the Accounting Standards Board in the United Kingdom, to expose the ‘Private Finance Initiative and Similar Contracts to FRS 5: *Reporting the Substance of Transactions*.’

## 1.2 Gatekeeper Power and Responsibilities

The political nature of regulatory processes has been discussed but there has been *'little attempt to consider formally the role of the exercise of power and influence in this process...yet an understanding of how, when and by whom power is exercised is widely recognised as a necessary pre-requisite of any rigorous analysis of the political process'* (Hope and Gray, 1982, p. 531).

Bachrach and Baratz (1970) identified two types of power within institutions. The first is the authority to choose between alternatives and secondly, as important, the ability to control the alternatives under discussion in the first place, for which the rationale behind a non-decision may be more important than the actual decision. Lukes (1974) extended these dimensions of power, drawing attention to powers concentrated in the hands of an elite and the manner in which their decisions are made because of lobbying activity. The institutional 'key player' board member or inside staff can add an issue, omit or defer an agenda item for consideration and then maintain control over the passage of that item within the political agenda itself (pp. 21-5).

Majone (2006) described, in a broader social context, the latter power as receiving insufficient attention, neglected even, where an individual or institution holds exclusive, or monopoly, power over the agenda. This power is reinforced by *'the uneven distribution of knowledge and manipulation of information, inter-institutional competition, and bureaucratic politics'* (p. 223). This is achieved through internal management of an issue and then by accepting, excluding or modifying external representations, including control by key staff over how a proposal is reported back afterwards. This can be crucial for understanding resulting policy outputs (pp. 229-32).

Young (1994) considered the issues that emerge onto the standard-setter's agenda as accounting problems and therefore appropriate for standard-setting action. These can then be presented as *'a solution to a problem'* (p. 86). Cobb and Elder (1983) had gone further by suggesting *'the impetus...for the definition...of a situation as a problem may come from the availability of a solution just waiting, if not actively searching, for a problem to "solve"'* (p. 177). Thus, the way in which an issue is defined technically *'when it reaches*



*the attention of the decision-makers may well delimit the range of alternatives subsequently considered. In fact, by the time it arrives at an actual choice point, its fate may already be decided'* (p. 30). Kingdon (1995) also suggested that solutions may precede problems.

For legitimacy, the standard setter needs to decide upon the appropriate response to an identified accounting problem, whether or not that solution is sufficient or simply reflects form rather than substance. Young (1994) postulated that the standard-setter employs a '*logic of appropriateness*' (citing Marsh and Olsen, 1989) in constructing responses to accounting problems. These are justified as '*getting the accounting right*' to facilitate accounting progress to allow '*accounting to become what it should be*' (citing Hopwood, 1987) *as well as eliminating what accounting should not be*' (Young, 1994, p. 86).

One aspect is the diversity of accounting practice and the appropriateness of allowing optional treatments in certain rules-based standards, *e.g.* by the FASB, in contrast to the IASB's preference to eliminate optional treatments entirely. Young (1994) suggests:

diversity in practice becomes a "problem" only when it is judged to clash with such accounting claims as relevance, reliability and representational faithfulness...[and] thus, diversity in practice is used to justify the inclusion of projects onto the FASB agenda and representational faithfulness is used to justify the designation of diversity in practice as a problem (p. 86).

Since setting accounting standards exhibits political and regulatory characteristics, it might be expected those standards will be grounded in precedence, subject to relevant, understandable, reliable and comparable qualitative criteria within a conceptual framework. Further acceptability might be established by academic or empiric research. Alternatively, it might be supposed that in order to solve an accounting problem, credence and widespread practical endorsement will be sought in support from preparers, users, academic commentators and the profession at large.

This might not be the case where insiders are the prevailing driving force. The more political and contested that process becomes the more likely the outcome will depart from principled criteria; whether because of successful submissions, lobbying activity, gatekeeper advocacy, or negotiated compromise.

Young (1994) argued that constructing an accounting issue as an accounting problem is not sufficient to ensure emergence of a project onto the standard-setter's agenda. These problems must be constructed and interpreted as appropriate duties and obligations for standard-setting action in response to the demands of a situation. The standard-setting process is *'heavily mediated by the language and the ways participants discuss an accounting issue'* (p. 88). By their use of language, or rhetoric (Weetman, 2001), key protagonists can reinforce their solution to an issue and, by their actions, disregard alternative representations from interested parties (Young, 2003).

In turn, Young's (1994) studies showed that *'agenda formation includes the interpretation of expectations about the role and purpose of the standard setters and is not a simple response to pressures from interested actors'* (p. 88). This purpose may include the aspirational criteria for the Mitnick (1980) archetypes to promote organisational reputation, advocacy, achievement, and survival. Alternatively,

standards setters [can] too often pull their punches, backing away from solutions they believe are best. Perhaps they do this because of a perceived threat to the viability of private sector standards setting, perhaps because of the sometimes withering strains of managing controversial, but needed, change, or perhaps because of a loss of focus on mission and concepts that are supposed to guide their actions (Sutton, 2002, p. 324).

Thus standard-setting agenda formation and responsibilities can involve complex political processes. The gatekeepers' role and actions, including responsiveness to change, are pivotal whether operating within their own regulatory agency, or beyond.

### **1.3 Accounting Standard-Setting Domains and Regulation**

Young (1994) suggested little was known about the background to *'changes in accounting practices in the financial accounting domain [which] often centre around recognition issues - when to recognise assets, liabilities, revenues and expenses'* :

changes in these practices may require the reporting entity to recognise "liabilities" previously excluded from the balance sheet, to delay the recognition of income or to hasten the recognition of expense. These accounting changes typically expand and enhance the domain of accrual accounting (and often historical cost accounting). The processes underlying these types of accounting changes remain largely unexamined (p. 83).

However, Young (1994), from studying FASB processes, cautioned that before considering the way an issue emerged and was considered, *'one must look beyond the*

*boundaries of [the] organisation and examine the broader space in which the FASB operates and accounting regulation occurs'* (p. 84). That regulatory space is an '*analytical construct [that] is defined...by the range of regulatory issues subject to public decision'* (Hancher and Moran, 1989, p. 277) In turn, this space is influenced by the domain's history and reflects political, statutory or transferred responsibilities devolved within national or international boundaries and associated regulatory requirements.

Using the regulatory space, or domain, metaphor, the standard-setter participants determine and prescribe particular reporting measurement or recognition procedures in order to decide the relevant form and content of an entity's audited financial statements within its jurisdiction. Hitherto that responsibility was defined locally, in the national domain; *e.g.* by the AASB in Australia or the Accounting Standards Review Board in New Zealand (ASRB-NZ).

However, from the mid- to late-1990s, supported by respective national standard-setting bodies, this responsibility increasingly shifted '*from home-grown standards towards worldwide ones'* (*Economist*, 2010, p. 72) through legislated harmonisation onto the equivalents of international financial reporting standards (IFRS). In the international arena this was initially the responsibility of the IASC, and from 2001, the International Accounting Standards Board, the IASB.<sup>5</sup> The latter's objective has been to obtain agreement to extend harmonisation of its global standards to seek convergence with standards issued by the FASB, together with the few other countries not already recognising IFRS. The objective is to become the recognised and accepted global accounting standards setter.

Although a standard setter issues accounting standards to refine or improve financial reports in the domain for which they are responsible, Young (1994) argued it is not a space where dramatic changes in accounting practice occur. Notwithstanding, some of the newer IASC and IASB accounting standards have resulted in significant financial and economic consequences for those entities subject to these standards.

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<sup>5</sup> The IASC was disestablished at 31 December 2000 and re-constituted as the IASB from 1 January 2001.

There is a need to understand the dynamics causing such outcomes. After all, such action can have profound impacts, *'it is within regulatory space that the content of these [FASB] reports, the timing of the recognition of profits and the amounts of the carrying values of assets and liabilities are decided'* (p. 85).

Young (1994) suggested reasons to consider accounting standard changes in this context – and others have offered similar comments. Young's first suggestion was to examine the participants in the standard-setting process. That is, not only the international standard-setting body itself but also its client country standard setters along with other external participants involved, such as lobbyists, auditors, users and preparers of financial statements. Even so, only notional recognition seems to be given to private sector 'users' of the information (Young, 2006), or in the public sector (Hay, 1994). However, Beresford (1993) expressed his frustration that users were not more active in FASB processes particularly as they are *'expert on what information would be most useful to them and why'*. He identified two possible reasons:

they don't derive as much benefit from financial reporting as we accountants have assumed, another is that some prefer the status quo, [but] absence of user involvement increases the risk the Board's decision-making [is insufficient]...they can help insure (*sic*) the Board's decision processes will be more balanced [and to] listen carefully to what they have to say (pp. 73-5).

Young's second suggestion, in contrast to Mitnick (1980) and Cobb and Elder (1983), was that it is not necessary to assume that special interest demands will give rise to proposals for changes in accounting standards being placed on the regulatory agenda: *'demands for accounting change may be unfocussed, lacking in specificity, and ambiguous'* (Young, 1994, p. 85).

Instead, insiders can initiate changes from within the regulatory body, with those changes reflected in board decisions and explained in introductory notes accompanying the issue of a proposed exposure draft, final standard or in subsequent amendments.

The converse can occur too. Internally, the board, with insiders, consistent with some of Mitnick's archetypes, can keep an issue off the agenda because it might threaten the concepts they espouse, or even their legitimacy and existence. Thus control of the issue definition and formal agenda processes are important potential elements of gatekeeper power and decision making to achieve desired ends.

Finally, drawing the above together, this *'metaphor of regulatory space demands that one pay closer attention to the actors and institutions that contribute to the processes of accounting change'* (*ibid.*, p. 86); that is, to the gatekeepers themselves operating within their mandated responsibilities and powers, and also to the territory, or domain, within which a regulatory body operates, relative to other agencies.

#### **1.4 Agenda Characteristics for Regulatory and Lobbying Activity**

The driving force for action by standard setters to solve an accounting problem may be derived externally, or stem from an internal institutional agenda. Each affects subsequent lobbying activity.

Cobb and Elder identified two types of general agenda characteristics:

- the “systemic agenda” described as being the full range of issues or problem areas that are both salient to a political community and commonly perceived as legitimate subjects of governmental concern. This systemic [political] agenda is not in any sense a formal agenda. It exists only in the sense that popular concerns, priorities, and values will both prescribe and proscribe the type of questions upon which authoritative decisions may be rendered; as opposed to
- the “institutional agenda” is much more formal [within a particular regulatory agency] and represents those items explicitly scheduled for the active and serious consideration of a decision-making unit...decision-makers may take action to [consider an item] on the agenda or decide to take no action (1983, pp. 160-1).

Cobb and Elder hypothesised that the greater the disparity between the two, the greater the intensity and scope for conflict within the political system and the more the likelihood for controversy and intensive lobbying activity. This will occur where one leads the other but with the tendency for the systemic, external agenda to lead the institutional agenda (p. 14). However this may not always be the case for accounting standards.

The systemic agenda may lead the institutional agenda in the standard-setting arena where external pressures from an accounting crisis or reporting scandal necessitate change by the regulatory gatekeeper (Peirson and Ramsay, 1983; Coffee Jr., 2006). How a decision-maker reacts in practice depends on the gatekeepers' archetypal role, including the continuing imperative to maintain regulatory legitimacy and reputation (Mitnick, 1980; Coffee Jr., 2006).

The institutional agenda, fostered by insiders, can lead the systemic agenda. An internal initiative may modify existing practice such that external parties recognise and accept that a proposal is relevant and timely. For accounting standard setting, that might occur because gatekeepers recognise existing standards need to reflect a new accounting practice or conceptual framework without any call for action from preparers or users. An example was promotion of ‘fair value’ by the IASC in the late-1990s<sup>6</sup> as opposed to ‘historic cost’ accounting, deemed more appropriate to reflect relevant financial measurement and reporting for users.

Alternatively, the regulatory authority may impose radical policies in advance of or different from the reality faced by the external community or other institutional agencies. In accounting, examples of the latter have been controversies over IAS 39 *Financial Instruments* leading to opposition from the European Commission, following lobbying by French banks, and the ‘fair value’ debate since the mid-2008 global financial crisis (Laux and Leuz, 2009). Another example, relevant to this study, was the industry response to the *Agriculture* standard which envisaged advanced accrued income recognition, unrelated to actual realisation. In addition, this risked taxable income recognition of unrealised, even hypothetical gains because the tax authority could regard application of approved accounting standards as acceptable in principle for identifying taxable income.<sup>7</sup> Thus a change in NZ-GAAP from adoption of the agriculture standard could have caused unrealised changes in agricultural asset and inventory fair values to be recognised for income tax determination.<sup>8</sup>

Intensive lobbying may be expected where significant economic interests are potentially at stake (Sutton, 1984). Doubts may be cast as to the appropriateness of the proposed standard, including its legitimacy. It may then be subject to reversal by parliamentary order or judicial review; the latter under general Administrative Law precedents if the standard setter did not follow all its designated consultation processes.<sup>9</sup>

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<sup>6</sup> For example: IAS 39 *Financial Instruments*, IAS 40 *Investment Properties* and IAS 41 *Agriculture*.

<sup>7</sup> In March 2004, the N.Z. Commissioner for Inland Revenue noted that if a profit is reported under the accounting standards, it is a *prima facie* reason to consider the reported profit eligible to be taxed.

<sup>8</sup> In the event, the N.Z. IRD specifically excluded unrealised ‘fair value’ income determination for *Agriculture* in favour of the traditional historic cost basis; but not for derived ‘fair value’ income in other standards, e.g. arising from the IAS 39 *Financial Instruments* standard.

<sup>9</sup> The right of a fair hearing, from the House of Lords decision in ‘*Cooper v. Wandsworth Board of Works*’ [1863] 14 CB [NS] 180, as developed in subsequent Australasian Administrative Law and High Court cases.

An important question therefore is how do issues gain access to the regulatory agenda and command attention before lobbying in response to a proposal begins?

If there were only a limited, non-specific demand for regulatory action, the supply internally of a general solution to an accounting problem is unlikely to be controversial. However, as Sutton (1984) and Young (1994) point out, supply of a proposed new standard with new measurement and reporting rules may lead to a novel solution affecting asset, liability and income recognition. Intensive political pressure and lobbying can be expected during formal agenda consideration stages; and/or afterwards, where practical experience indicates deficient concepts.

Cobb *et al.* (1976) described three models of agenda building. The *outside initiative* model corresponds broadly to the systemic agenda outlined above. Initiatives originate for consideration from sources external to the regulatory agency. The *mobilisation* model and the *inside initiative or inside access* model are apposite for this study. Under the *mobilisation* model gatekeepers initiate policy but seek prior support from constituencies for implementation. The *inside access* model describes agenda building and policy formation processes where proposals generated within the regulatory agency are coupled with limited effort to involve general participation by public constituencies. They suggested these models may occur in combination, or sequentially (pp. 135-7).

Relevant for this study, Jones *et al.* (2000) used the Cobb *et al.* (1976) models in their analysis of the political processes surrounding the CLERP-1 reform programme initiated by the Australian Government. This programme included the then controversial step of controlling local accounting standard setting by mandating adoption of IASC standards over those of the AASB. Stoddart (2000) also described the political and practical implications of these changes for the AASB, for corporate and other lobbyists, and for other stakeholders.

### **1.5 Lobbying and Lobbyists**

Gatekeepers are not immune to external lobbying. Walker and Robinson (1993, p. 9) note little attention is given to the identity of gatekeepers who control the rule-making agenda

and what prompts their consideration of lobbying issues as opposed to the ample number of reports on lobbyists' responses and submissions on proposed accounting standards.

Lobbying may arise internally within the regulatory body through formal and informal insider lobbying to promote a preferred solution or it may be evident from outside influences and lobbying.

External lobbying will be obvious from direct submissions, mobilisation of special interest groups, media exposure, judicial proceedings, parliamentary or regulatory inquiries into past scandals, or it may arise from academic and general commentary on practitioner or user concerns. Each party will seek formal recognition that an issue warrants gatekeepers' attention to be placed on their agenda and then lobbying to influence the passage of their preferred solution by written, verbal or private representations. The reasons for external lobbying are many. Submissions may favour a proposal, but lobbying action opposing or to amend a proposal may stem from a lobbyist's economic self-interest and concerns about the proposal's potential impact on their general or specific activities (*e.g.* Mitnick, 1980; Sutton, 1984; Young, 2003).

Walker and Robinson (1993), and Hodges and Mellett (2004), suggest that informal lobbying may be as relevant as formal lobbying. But, being private to the regulatory body, its content and impact is less susceptible to analysis - unless support papers and meeting minutes are made available or if individuals concerned are interviewed. Any such lobbying activities will be on an informal basis if originated amongst staff or members of a regulatory body, or between staff or members of different standard-setting bodies.

Published empirical studies of lobbying in relation to accounting issues (*e.g.* Watts and Zimmerman, 1978; Dhaliwal, 1982; Sutton, 1984; Deakin, 1989; Larson, 1997; Hodges and Mellett, 2004) have been possible because of publication of issues papers or draft standards. But these studies do not attempt to identify the extent to which internal deliberations occurred previously or how an issue ever reached the conclusions expressed in published exposure drafts. Such studies rely upon the written evidence of lobbying submissions, although Hodges and Mellett (2004) did conduct interviews of key U.K. Treasury officials in support of their findings on informal lobbying. Respondents to



exposure drafts either support, or comment upon matters defined for discussion by the standard-setting agency. These studies are consistent with the *mobilisation model* whereby gatekeepers initiate policy then seek support from constituencies prior to implementation.

In calling for submissions, the way a question is presented can influence the structure and content of submissions received. Qualified requests for submissions and the phrasing of those questions is a manifestation of power over the standard-setting process. The ‘*rhetoric*’ of drafting responses on those submissions affects the quality of the debate and its subsequent consideration (Weetman, 2001; Young, 2003).

Since many written submissions are public, and verbal submissions may or may not be, much emphasis is given in the literature to ‘*actions “interested parties” take to influence the rule-making body, collectively referred to as lobbying*’ (Sutton, 1984, p. 81).

Lobbying normally follows release of formal discussion papers and exposure drafts, with submissions made on those drafts. But it may continue afterwards following release of commentary supporting issue of an approved standard. Later publicity in company reports or in academic or media articles may also influence the standard setter to initiate change.

Typically a discussion paper is crafted to call for a response whether a particular aspect, interpretation or specification is agreed upon, but with opportunity to add further comment.

Where lobbying is viewed by insider staff as a pluralistic voting exercise it is only ‘*a rudimentary statement of preferences*’ (Walker and Robinson, p. 11). The tallies may be interpreted by staff and presented to the regulatory body as equivalent to ‘votes’. These can be open to ambiguous interpretation, *e.g.* where it is not clear whether a response is on a point of principle or simply a drafting matter. Sometimes, the submission voting count is discounted if considered collusive, *e.g.* from a write-in campaign (Dyckman, 1988). If not discounted, conclusions drawn from the *quantum* of raw votes may be over-simplified.

Internal staff analyses of submissions can include a further sifting process where the reputation or presumed knowledge of a submitter, or group of submitters, is given greater weight over others whose views may be equally relevant. What is germane is not the

quantity of votes made on submissions; rather, the extent to which representations expressed about a proposal address matters of principle, propose material corrections or offer a reality check on implementation or practicability. Therefore, to assist interpretation, it is necessary to identify whether a respondent expressed a preference or made a substantive argument for or against a proposal. Then, as an overlay, how the insiders exercised their power to add, amend or omit that issue during their deliberation process. This may be made evident by amendment to the original text.

Other interpretive evidence may be found in the summaries and arguments provided in published notes as to whether and how the gatekeepers considered a lobbying representation and the reasons given for its adoption, or rejection.

### **1.6 Who Lobbies, and Why**

In Young's (1994) analysis, lobbyists may be found amongst a wide range of interested stakeholders. Depending on the scope and impact of a proposed standard, they might involve other regulatory bodies; the profession, including auditors and practitioners; preparers of financial statements; users, including investors, analysts and financial institutions; creditors; academics or other stakeholders, *e.g.* employees.

The advent of the IASC/IASB has resulted in a wider community of potentially interested lobbyists than previously experienced in a national domain. These now extend to national standard setting bodies, international financial regulators and trans-national organisations - such as, the International Organisation of Securities Commissions (IOSCO), International Federation of Accountants (IFAC), the World Bank or the European Commission (EU).

However, a feature of supra-national IASC/IASB standard setting is that traditional national standard-setters' responsibilities generally reduce to becoming a standards taker. They are left with qualified power to effect non-compliance amendments for jurisdictional purposes or over non-IFRS reporting entities, *e.g.* for the public and not-for-profit sectors.

On the other hand, new degrees of freedom can result. National standard setters can lobby international bodies direct to maintain their own legitimacy or to seek acceptance of

their preferred practice. Alternatively, regulatory agencies may transfer a problem from one domain to another to deflect local controversy by reference elsewhere for guidance or interpretations, *e.g.* to IFRIC, the IASB, or the G4+1 forum. That is, anything not achievable locally '*may be achieved by international cooperation*' (Majone, 2006, p. 241).

Whilst Walker and Robinson note that accounting academics might be expected to have greater familiarity with technical issues and '*a comparative advantage in participating*' (p. 19), there appears to be only a low participation rate in standard-setting processes. This is not for lack of requests (Beresford, 1994). But reasons given for not doing so include lack of time or resources, inadequate academic rewards for this activity, and the technical nature of the issues (Tandy and Wilburn, 1996). It may also reflect a realistically low expectation of ability to influence decisions by the gatekeepers, including their key staff. Accordingly it is necessary to look elsewhere.

Sutton's (1984) 'Downesian' analysis into lobbying was conducted from an economic and financial perspective.<sup>10</sup> Just as the standard setter should consider an overall economic cost/benefit analysis, he discussed the factors behind a lobbyist's economic cost/benefit analysis. This is conditioned by the lobbyist's benefits-calculus on whether or not to lobby, and whether the probability of influencing the decision process exceeds the actual and opportunity costs in undertaking such lobbying activity. Any results expected must also outweigh benefits from 'free-riding' on the lobbying efforts of others to achieve a lobbyist's preferred outcome (p. 82). Given the time and total monetary and opportunity costs involved '*only those who expect large financial benefits from the activity will lobby, other things being equal*' (p. 85). Thus lobbying will occur from those for whom the effects of a new or changed standard are likely to be most profound.

A preparer of financial statements will be directly concerned with the outcome, and has more at stake compared to users generally. A preparer can more easily focus upon, justify and finance lobbying activity. '*For these reasons action by the regulated is likely to be better organised, funded and informed*' (Mitnick, 1980, p. 134). This may include support for the *status quo* or, instead, lobbying for alternative accounting treatments. A rational

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<sup>10</sup> Refers to Anthony Downs' (1957) analytical approach to political science and his single-period economic voting model relevant for Sutton's economic analysis of lobbying intentions and activities.

lobbyist will try to mitigate real and opportunity costs. The lobbyist might consider strategies such as cost-sharing, *e.g.* by using or funding an industry association to make submissions on his behalf. Fewer than expected entities lobby themselves, preferring intermediaries (Kenny and Larson, 1993).

An obvious intermediary is the entity's auditor or one of the major accounting firms. They have an added rationale for being seen to make submissions so as to emphasise professionalism, including that of their technical departments. The major accounting and auditing firms are ideally positioned to promote change as agent on behalf of their client base (Deegan *et al.*, 1990). They can also exhibit professional loyalty to the accounting standard-setting body in support of new or revised standards. There is a further benefit where changes potentially increase auditing or advisory fee income, *e.g.*, as an outcome of adoption of the new international financial reporting standards (Sutton, 1984, pp. 88-9).

Like Young (2003), Sutton distinguished between preparers, who are more likely to be concerned with economic impacts altering '*measurement of earnings or valuation of assets and liabilities*' and '*consumers (who) supposedly pay more attention to standards which alter the level of financial disclosure, favouring those which provide additional information*' (1984, p. 87). The latter applies particularly where the user, government agency or regulator bears no direct cost for supply of information. Thus there is less inhibition in seeking extended disclosures.

Adverse preparers' reaction can occur where business model confidentiality is at risk or where costs of disclosure exceed reasonable information supply relative to other standards. The preparer therefore has a greater vested interest to lobby where the incremental costs from a change in the *status quo* or from supplying information for public benefit exceeds any perceived commercial private benefit.

Where the object of lobbying is to '*influence the content of existing or proposed standards*' (*ibid.*, p. 89) then, from the lobbyist's perspective, early intervention direct, or associated with others, can carry higher chances of reward by effecting change at lower cost. Failure to effect early change does not pre-empt later opportunity to extend lobbying activity during future consideration phases. Lobbying effectiveness can be evidenced by

the extent to which significant requested changes occur as a proposed standard matures. These may be due to gatekeeper responsiveness to external public submissions – from preparers or users – or deduced as evidence of internal lobbying – whether by staff, technical advisers, standard-setting agencies, or from confidential submissions.

The gatekeepers themselves can seek to mitigate lobbying and potential adverse criticism from their colleagues and financial statement users and preparers. These strategies may be achieved, for example, by issue of pre-exposure drafts to test a new proposal and gauge the scale and type of reaction to be expected during the formal ‘Exposure Draft’ deliberative phase. Alternatively, they may announce intentions to initiate field test surveys with preparers, accounting firms and other users to determine the feasibility of a proposed accounting standard; or, to propose a post-enactment review to determine actual experience after adoption of an accounting standard.

Finally, inter-agency lobbying to influence a desired outcome may occur or between standard setters, as in the case of the AASB and the IASC for *Agriculture* or between Government agencies and the standard setters, *e.g.* the APB and SEC for *Accounting for Income Taxes*. Few instances of the latter are recorded, but some include the discussion of interaction between Australian government agencies and a standard-setting agency described by Walker (1992), conflict between Australian public- and private-sector agencies (Walker and Robinson, 1994), and similar interactions between the FASB and the U.S.A.’s SEC (with three examples cited by Walker and Robinson, 1993, p. 6.).

## Chapter 2. CASE STUDIES: RATIONALE, DESIGN AND OUTLINE

### 2.1 Case Study Objectives and Research Questions

Walker and Robinson suggest scope for research about particular issues placed on the formal agenda of rule-making bodies:

little is known about the process of agenda formation: how some topics are selected for consideration, while others are not; how issues are pre-filtered before proposed rules are publicly exposed; or how regulatory agencies come to draft rules tightly or loosely...case studies, in particular, might provide a better understanding of the influence of different interests in shaping regulatory agendas, and the methods used to secure agenda entrance...[and] it appears likely that case studies may highlight the role of “key players” in those process(es) (1993, pp. 30-1). [*N.B. Emphasis added*].

This chapter describes the case studies that were undertaken to examine the proposed new rules regulating financial reporting by agricultural entities. The proposed rules were promoted during the decade from the mid-1990s by the Australian and International standard setters respectively and, subsequently, adopted in Australia and New Zealand.

Yin describes the rationale for adopting a case study methodology. It is particularly relevant as an explanatory research strategy to answer ‘how’ and ‘why’ questions (2003, pp. 5-10), such as those outlined above and in Section 1. The definition of a case study, citing (Schramm, 1971, December), ‘*is that it tries to illuminate a decision or set of decisions: why they were taken, how they were implemented and with what result*’ (p. 12). It is likely to be favoured in examining contemporary events, be reliant upon multiple sources of evidence, and where the objective is to collect, present and develop data found within its real-life context.

The case studies consider each of the internal agenda entrance, technical and phased political processes and gatekeeper deliberations on the proposals; together with lobbying on and issue of respective standards. These studies are supplemented by examining the introduction of these standards, and subsequent experience in Australia and New Zealand, including the AASB’s post implementation review.

As an overview, the research could be described as a variation of the multi-issue/multi-period corporate lobbying study (Georgiou, 2005). The focus is on ‘key players’, and lobbyists, for all rule-making phases for two agriculture standards across the three (IASC, Australian and New Zealand) domains. It offers insights into the ‘how’ and ‘why’ activities when the ‘key players’ were establishing agenda entrance, throughout their consideration stages and how inter-agency positioning influenced a desired outcome for objectives not met through co-operation. These processes have not been examined before.

In summary, the objectives and principal research questions are to examine:

- why and how the AASB’s *SGARA* and IASC’s *Agriculture* topics gained access in respective regulatory domains;
- how each topic progressed through each of the respective rule-making stages;
- who were the key insider gatekeepers controlling the respective agendas; and
- how respondents reacted to the proposals, and the gatekeepers’ responsiveness.

## **2.2 Research Design**

The study relies upon the classification of agenda-building and rule-making processes described by Cobb and Elder (1983), and uses as a framework the summary of accounting rule-making activities set out in Table 1 from Walker and Robinson (1993). This model assists consideration of the ‘*little examined*’ early agenda access and entrance stages from existing practice to establishing new standards through all agenda processes; and thereafter, actual practice and experience. There were opportunities for ‘*policy-learning*’ from evidence-based exposure draft submissions; from evaluation of potential policy revisions from the IASC’s Field Test in 2000; or, from the AASB’s PIR for its *SGARA* standard in 2003.

Departure from existing practice may be evolutionary. It may arise from experience and greater understanding - for which incremental change is appropriate. However the accounting changes introduced by the *Agriculture* standards were far more consequential and revolutionary. The research therefore seeks to describe the nature of these changes.

The accounting and reporting changes were novel since, *inter alia*, existing accounting standards specifically excluded accounting for biological assets and revenues. The pre-IAS 41 standards for IAS 2 *Inventories*; IAS 16 *Property Plant & Equipment*; and IAS 18 *Revenue* each excluded initial recognition of agricultural produce or changes in fair values of agricultural assets. These are summarised in [Appendix 1](#).

Accordingly, over many years numerous local accounting rules, guidelines and approved accounting procedures were developed for accounting treatments for general and specific agricultural sectors worldwide, as recorded in [Appendix 2](#). This was in addition to the use of existing standards as a default option. For a preparer or user, all carried the *imprimatur* of generally accepted accounting practice with authoritative support.

The effect of the new agriculture standards was to resolve this policy *lacuna* by first proposing an omnibus standard for all agriculture sectors. The research approach adopted here enables the identification of what occurred at each rule-making stage in each domain and the involvement of the gatekeeper initiators who designed those new rules. The Table 1 elements-categorisation below enables a systematic examination of sequential phases in the rule-making process, and the trans-national interactions across both the Australian and IASC regulatory domains.

Evidential sources for the study could not come from publicly disclosed formal meeting minutes. There were none; since neither the Australian AARF, or the AASB, nor the IASC published minutes of meetings during the examination of the *SGARA/Agriculture* standards, up until 2000. Instead, prime source material was found in respondents' external submissions at each agenda stage and in official summaries of responses reported at the next agenda development stage. These were supplemented by staff articles recording progress in IASC in-house journals and by Project Manager's commentary in published articles. Another important source used was information received from access to private papers, letters and reports; from the Camfferman and Zeff (2007) history of the IASC; from academic journal articles and preparer's annual reports; and from significant unpublished material released by request to the IASB and the AASB.



### 2.3 Agriculture Project Outline

This outline summarises the establishment of the new AASB *SGARA* standard in Australia and separately, virtually in parallel, the IASC's *Agriculture* standard. The point of departure from existing practice is discussed in Section 3. The progress through each rule-making stage is then described in Section 4 through to issue of respective AASB 1037 and IAS 41 standards; and then, in Section 5, the latter's transfer to Australia and New Zealand.

Adapting the Table 1 methodology, Table 2 provides a chronology of when formal documents were released, and the number of submissions made on each, at each stage.

***Table 2. Development of the Agriculture Standards***  
**Summary of Formal Agenda Elements Chronology and Lobbying Submissions**

Section	Elements	Australia	International	New Zealand
<b>3</b>	<b>Existing Best Practice</b>	<b>2 + Papers</b>	<b>Surveys</b>	<b>12</b>
<b>4.1</b>	<b>Discussion Memo/Paper</b> Internal to AARF & IASC	<b>Project Brief</b> [July 1990]	<b>Point Outline</b> [March 1996]	-
<b>4.2</b>	<b>External Document</b> Date <b>Submissions</b>	<b>DP 23 SGARA</b> [May 1995] <b>4</b>	<b>DSOP Agriculture</b> [December 1996] <b>42</b>	
<b>4.3</b>	<b>Exposure Drafts</b> Date <b>Submissions</b>  <b>Field Study [unpublished]</b> <b>Submissions</b>	<b>ED 83 SGARA</b> [August 1997] <b>46</b>	<b>E65 Agriculture</b> [July 1999] <b>61</b>  <b>FTP [March 2000]</b> <b>18 [out of 84]</b>	<b>ED-90</b> [April 2002] <b>100 [197]</b>
<b>4.4</b>	<b>Standards Issued</b> Date	<b>AASB 1037</b> [August 1998]	<b>IAS 41</b> [December 2000]	
<b>5</b>	<b>Transfer IAS 41....as EDs to:</b> Date Submissions <b>New IFRS Standards issued</b> Date	<b>ED 114</b> [May 2003] <b>20</b>  <b>AASB 141</b> [July 2004]		<b>ED NZ IAS 41</b> [July 2004] <b>12</b>  <b>NZ IAS 41</b> [November 2004]
<b>6</b>	<b>Post-Enactment Review</b> <b>[unpublished]</b> <b>Replies</b>	<b>PIR</b> [May 2003] <b>28 [out of 109]</b>	-	

Source: Adaptation of Table 1 Stages based upon Walker & Robinson Table 1, p.7.

The Agriculture project began in Australia when the AARF, as adviser to the AASB standard-setting body, decided to sponsor research under a tightly defined *Project Brief* for what became the *SGARA* Discussion Document No. 23; undertaken by contractors at The University of New England (UNE). In parallel, the AARF undertook its own research project, sponsored by Robert Keys, as an AARF insider, co-funded by the Australian Government's Rural Industries Research Development Corporation (RIRDC). Despite repeated requests, only the Abstract to that research project is available.

Independently, in the early-1990s, the IASC decided to turn its attention from its Core Standards then being developed for approval by IOSCO. This included agriculture as a specialised accounting topic. Notwithstanding being one of the most prominent worldwide economic activities, agriculture had been a neglected area and was generally excluded from approved accounting standards. Formal consideration was propelled onto the IASC agenda by a generous World Bank grant due to the Bank's trans-national responsibilities to fund agricultural projects in underdeveloped and newly-developing third world economies.

Accordingly, in 1994, the IASC established a working party to consider how agriculture might be brought within mainstream accounting standards. In 1996, the internal Steering Committee, appointed for this task, presented to the Board a *Point Outline* which was subsequently converted into an approved *Draft Statement of Principles* (DSOP). The DSOP set out the issues, the alternatives considered and proposals for resolution. The IASC invited comments. Some concerns were expressed by accounting bodies and practitioners. Only five agricultural entity preparers worldwide responded.

Meanwhile, during the IASC's DSOP consideration process, the AASB released its *SGARA* ED 83 Exposure Draft in August 1997, and then, following review of submissions, formally issued its AASB 1037 *SGARA* standard in August 1998. This was to come into effect for the financial year ending 30 June 2000.

There was widespread lobbying by preparers and the profession. They sought to postpone the commencement date to gain sufficient time to develop adequate accounting and computer systems to capture relevant reporting and disclosure information required under the new standard. In July 1999, the AASB issued AASB 1037A which deferred the

commencement date to financial years commencing on or after 1 July 2000, with early adoption encouraged.

In July 1999, the IASC released its Exposure Draft E65 for comment by 31 January 2000. Because of the lack of sector submissions received, the IASC Board recognised the need for further input. It approved a Field Test Project (FTP) in March 2000 to seek practical advice from experienced commentators and preparer companies about the proposed 'fair value' measurement principles. The results of this FTP were not published.

Following further internal debate, and three further meetings, the IASC Board finally approved IAS 41 in December 2000 as virtually its final act prior to the IASC being disestablished and re-incorporated as the IASB. The effective IAS 41 implementation date was for financial reporting periods commencing on or after 1 January 2003.

After further lobbying, the effective date was deferred in Europe until 1 January 2005 and as a result elsewhere.

The AASB was obliged to expose the Australian version of IAS 41 as a new standard when it announced convergence to IFRS with effect from 1 January 2005. The associated ED 114 Exposure Draft, issued in May 2003, required further local consultation to substitute for AASB 1037. This had been operating for just two years. The harmonised international standard was issued in July 2004, as AASB 141 *Agriculture*.

Simultaneously with ED 114, the AASB undertook a post implementation review on its AASB 1037 *SGARA* Standard. This was a first. The rationale was to recommend to the IASB any desirable changes to IAS 41 before the formal 1 January 2005 implementation date. The AASB's recommendations were not published, but are discussed in [Section 6](#). Some were transferred to IFRIC for further consideration. However, one recommendation was very significant. This was to split IAS 41 into two. Its effect was to reverse a major AASB *SGARA* concept. The IASB has ignored this recommendation to date.

In New Zealand, the FRSB issued its ED-90 *Agriculture* in March 2002. This was virtually identical to IAS 41. ED-90 received a record number of submissions. The

number varies from 100 to 197 depending on how responses are tallied. Most were critical. The irony was that few of the respondents would be affected until such time as the IASB's *Small and Medium-sized Entities* (SME) standard was approved for local application.<sup>11</sup>

Two years later, in October 2004, FRSB staff issued their analysis of ED-90 submissions. Notwithstanding the weight of critical submissions, and despite reservations, the FRSB recommended adoption of NZ IAS 41, without amendment, effective for accounting periods commencing on or after 1 January 2007, consistent with its objective to harmonise NZ-IFRS accounting standards with Australia.

However, as a possible concession to submitters' lobbying efforts, the FRSB noted a concurrent legislative proposal to permit differential reporting exemptions below reasonably high reporting thresholds. In their transmittal advice to the IASB, the FRSB recommended specific matters be referred for review by IFRIC, or by the IASB itself.

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<sup>11</sup> IFRS for *Small and Medium-sized Entities* was eventually approved by the IASB in July 2009. It has not been accepted yet as applicable in either New Zealand or Australia.

## 2.4 Summary

This section has identified the regulatory agenda entrance and lobbying literature and political and lobbying processes surrounding issue of a new accounting standard. Hitherto, little attention was given to the role of gatekeepers and key insiders in these processes. This research topic does so.

Using the development of the *SGARA/Agriculture* standards by the AARF/AASB and the IASC respectively, the following case studies utilise the classification of stages in the development of regulations identified by Cobb and Elder (1983) and the institutional rule-making processes in accounting regulation summarised by Walker and Robinson (1993, Table 1).

This topic covers more than technical accounting design. It also addresses the role and identity of ‘key players’ involved. These proposals were accompanied by significant lobbying activity from preparers and users across the Australian and International domains; subsequently to be repeated, following convergence of IAS 41 *Agriculture* in Australia, and on harmonisation in New Zealand.

The AASB and IASC *Agriculture* standards provide some of the most comprehensive worldwide source material for evaluating a unique sector standard. None of this information has been analysed to date in its totality as a case study. It supplies insights into how these various processes were undertaken in practice, and as each became inter-twined. Traditional accounting-standard lobbying processes have become more complex due to changes in institutional arrangements following the establishment of the IASC/IASB and IFRIC bodies. They have created a new extra-territorial dynamic.

To foreshadow what is to follow: this study examines how former national standard setters variously became ‘insiders’, lobbyists to, or ‘standards takers’ from the IASC. These impacts have not been discussed before; although interaction between Government and standard setting agencies was discussed *e.g.* by Walker (1992).

### Section 3. TECHNICAL LITERATURE & HISTORICAL ACCOUNTING PRACTICE

#### Introduction

This section provides an overview of historical professional developments and accounting concepts for agricultural sectors in England, Australia and especially in New Zealand. The variation in agricultural accounting practice and reporting revealed the wide diversity in historical cost accounting more generally. These provide a reference to help identify the accounting ‘problem’ requiring resolution.

The predominant form of accounting was special purpose accounts for family farming entities. These were prepared for proprietorship, trust or individual business purposes, including for taxation. They reflected recommended accounting practice suitable for a specific agricultural sector, *e.g.* for bloodstock or horticulture. However, from the 1970s onwards, the emphasis shifted towards ‘current value’ accounting. This was a period of rising inflation.<sup>12</sup> Farming entities became larger scale businesses. They required more sophisticated management reporting to facilitate external financing, especially once Australasian agriculture diversified away from traditional arable and pastoral farming.

Since there were no formal accounting standards for reporting by listed agricultural entities in Australia or New Zealand, respective national accounting bodies established guidelines to provide ‘best practice’ recommendations for practitioners and users. With the exception of forestry, the few publicly listed agricultural entities often adapted existing general purpose accounting standards for their financial reporting.

There were no formal guidelines for forestry. The listed forestry companies were large enough to develop their own accounting policies and reporting practices virtually independently of each other, thereby presenting financial statements lacking in consistency and comparability. This was best exemplified by the reporting practices adopted by NZ Forest Products Ltd and by Fletcher Challenge Ltd. The latter had also to respond to different New Zealand, Australian and US-GAAP reporting requirements.

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<sup>12</sup> As a result, and beyond the scope of this study, were the various inflation-adjusted accounting proposals developed in many countries about that time.

### **3.1 Historical Background**

The mid-18<sup>th</sup> Century in Britain marked a transitional phase for agriculture. It was changing to a quasi-commercial basis able to provide extra food for the growing urban and industrial population. Resources were also freed from subsistence farming to provide factory labour for the nascent industrial revolution. A contemporary feature was the development of double-entry book-keeping '*wherein the medieval goal of subsistence was replaced by the capitalist goal of profit...through enabling the measurement of a proprietor's capital [and] calculation of periodic profit*' (Edwards *et al.*, 2009, Table 4).

Edwards *et al.* noted that changes in simple book-keeping towards more informational double-entry accounting occurred '*with several purposes of accounting identified in the early treatises [namely] – accounts as a means of establishing financial position; accounts as a means of measuring profitability and changes in financial position...and the use of accounts for performance assessment and decision making*' (2009, p. 2).

These resonate in a later detailed history of book-keeping practice for British farming activities prepared at the beginning of the 20<sup>th</sup> Century (Ronaldson, 1903).

This practice reflected proprietorship or, more generally, special purpose accounting. The aim was to provide an annual measure of stewardship over farming and husbandry activities for country estates, landlords or tenants. Quaintly but simply, they had two purposes: first '*to set forth in a plain and lucid manner a man's (sic) assets and liabilities*'; and, second, '*to show clearly and distinctly in the books the changes on a man's property*' (*ibid.*, p. 480). The measures were mainly cash-based and covered basic aspects of traditional arable and pastoral farming, primarily for arable crops and livestock.

The book-keeping comprised prime entry records, day journals and double-entry accounts. These enabled compilation of the annual trial balance, profit and loss account and balance sheet so as to determine, periodically, '*the capital invested in the farm*' (*ibid.*, p. 480).

Although anachronistic in today's terms the references were to then-current farming products and practices, such as *steelbow*, *chats* and *stirks*, and with separate ledger accounts held for *horses food*, *farmyard manure [fertiliser]* and *un-exhausted improvements*.<sup>13</sup> Appropriate to the time, horses were treated as capital stock carried at depreciated historic cost, analogous to other farmyard implements.

This early practice had one special feature. Because of the seasonal over-lap, each annual harvested crop was treated as the overall annual profit record because of the '*one difficulty in farm book-keeping, and that is, that there is no date in the year when one crop is realised before large expenditure [is spent] on the next*' (*ibid.*, p. 480).

The preferred balance date was end-October, being nearest to Martinmas, marking the traditional end of autumn. At the end of that annual accounting period, revenue was recorded at the estimated realisation valuation at harvest, excluding any associated marketing costs. These were accrued as a liability. The direct and indirect costs of growing and using the crops, including materials for own-use or as payments-in-kind to farm workers, were carried as expenses direct to the profit and loss account for the year so as to determine the net outcome of the farming activity for that year. If, subsequent to harvest, but within the Martinmas accounting year, any sales occurred at greater- or less-than the estimated harvest realisation, the resultant net realisation was adjusted within the crop-inventory carrying value in the balance sheet.

Ronaldson then described the procedures for the following year.

As inventory was sold, the previous year's balance sheet crop-inventory value and the respective cattle, sheep and swine livestock-inventory values were depleted progressively at actual net sales realisations. Own-use of crops and any payments-in-kind were charged at assessed progressive current valuations when withdrawn from inventory accounts.

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<sup>13</sup> *Steelbow*: crop belonging to landlord which tenant receives free when entering farm but has to leave equivalent final crop in place, without payment, at end of lease;  
*Chats*: small, poor quality potatoes;  
*Stirks*: one- to two-year old heifers or bullocks.



At year-end, following the harvest year, the balance remaining was then transferred direct to capital account, rather than as a debit or credit against the then current year's harvest being recorded in the profit and loss account. Thus the prior year's profit was finally determined after netting off all subsequent own-use and third party net realisations.

These '*general principles of book-keeping...[enabled John Smith, the]...East Lothian farmer<sup>14</sup>...to show the profit or loss from each year's crop, and the books, if not so elaborate, were on the same lines as the books kept by a manufacturer in his counting-house*' (*ibid.*, p. 513).

Even a century ago, special seasonal features and hazards of farming were acknowledged since '*the varying seasons also affect the different crops in different ways*'; therefore, without some financial analysis, the farmer '*can have only a very general idea which crops pay him best to grow, or rather what system of cropping is most advantageous for him on his special farm...and the costs of the various crops*' (*ibid.*, p. 514).

These accounts were thus annual special purpose proprietorship financial and operational double-entry records. They were unlikely to be intended for use by third parties. However, they were equivalent in purpose, substance and form to the merchants' accounts described by Edwards *et al.* (2009).

There are few references available on traditional livestock accounting. In Australia, an encyclopaedic treatise *Station Book-keeping for Pastoralists and Farmers* (Vigars, 1937) provided recommendations for double-entry accounting records. These included the various source journals and predominantly cash-based ledger accounts necessary for ordinary station purposes, comprising grazing and farming business ledgers. These were kept separate from any commercial property and financial investments and proprietorship financing activities.

Specific ledger accounts were detailed for Sheep, Cattle, and Stud respectively. These were multi-columnar ledgers for number, age, description by type of animal, prices paid,

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<sup>14</sup> South-East Scotland: from Edinburgh south to the border with England.

and costs or sales proceeds with reconciling quantitative sub-sections for purchases, births, losses and deaths, own-use rations and sales respectively. The only unusual item was accounting for 'Natural Increase'. No value was ascribed until valuation of stock on hand at balance date; sometimes quarterly, but mostly only annually. Thus '*profit from Natural Increase [for cattle and sheep] finds its way into the profit and loss account, although not realised upon*' (Vigars, 1937, p. 16). Inventory valuation measurement was not defined but appeared to be an attributed net market value or, in one example, at cost.

The traditional initial inventory net valuation-at-harvest concept became the basis for the new *SGARA* standard in 1998, whilst market valuation at balance date was developed by the IASC in 2000. Eventually, in 2004, IFRIC determined that selling and transport costs should be deducted from market prices to measure net fair value at the farm gate.

The dichotomy of performance and wealth reporting, or some combination of the two, as described by Ronaldson reappeared a century later. The proposed methodology, developed from arable and pastoral applications, which recognised unrealised inventory and asset values in the income statement, proved to be controversial when subsequently extended to all agricultural financial reporting, especially for bearer-entities.

### **3.2 Evolution of Agricultural Accounting Best Practice in Australasia**

Prior to the First World War, as in Britain, farming financial records would have been primarily proprietorship accounts for the individual farmer, partnership or trust farming entity, similar to those described above. In both Australia and New Zealand, the predominant agricultural activity was sheep or cattle pastoral farming for meat and wool production, coupled with associated cropping for supplementary feed. In Australia other major cropping regimes included wheat, sugar cane and some viticulture.<sup>15</sup> In both countries there were thriving stud and blood-stock industries.

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<sup>15</sup> An important distinction overlooked when the new standards were being developed was the difference in agricultural activity definition between *viticulture* - the cultivation of vines and grape-growing for sale as produce - and *viniculture* - the cultivation of grapes for the production of wine.

The other principal farming activity in New Zealand was the supply of milk from dairy farms to farmer co-operatives for butter and cheese manufacture for export. This started in 1882 following the success of refrigerated shipping for meat and dairy product exports, principally to Britain (Duncan, 1933).

In 1916, New Zealand farmers were required to pay income tax for the first time (Smith, 1974; Glasgow 1975).<sup>16</sup> As a result, cost-based production and inventory valuation principles became a key element in maintaining accounting records and for fiscal income determination when preparing the annual income tax return.

The inter-war years were a period of rising, but fluctuating livestock prices (Fippard 1948, p. 6). Consequently, significant unrealised annual income variations ensued and could be '*disastrous in rising prices with graduated tax scales*' (*ibid.*, p. 48). In these circumstances, the New Zealand tax authority devised livestock age-class standard values for fiscal inventory-valuation. Initially, these were market-value equivalent proxies; but they tended to reduce in value over time (Glasgow, 1975, p. 6). In effect, fiscal income determination was related to net realisations coupled with net inventory standard carrying-value adjustments where livestock numbers progressed through successive age-classes (Smith 1974, pp. 14-15). These standard values were accepted as best accounting practice, but market values were still required for stud stock (Plank, 1947, pp. 3-4).

Until the 1970s, standard values were institutionalised by Australasian judicial decisions for farm estate probate purposes and for family farming trusts. These judgements provided generally-accepted accounting valuation rules, and practice, to determine income and 'fixed' and 'floating' capital between trustees, life tenants and remainder-men (Free, 1940; NZSA, September 1991).<sup>17</sup>

From the end of the Second World War, agricultural entities in Australasia experienced major growth to restore farm capacity and meet food shortages (Fippard, 1948, p. 7), and for export-led growth associated with the 1950s Korean wool boom.

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<sup>16</sup> Graduated land tax was introduced in 1892 based on unimproved value of farm land (Fippard, 1948, p.5).

<sup>17</sup> *E.g.*, In Re Walker (1901) 1 N.S.W.S.R.237; In Re Angas (1906) S.A.L.R.140; In Re Bassett [1934] N.Z.L.R. 690; for other Australasian cases - refer Free (1940) and Smith (1974, pp. 11-13).

Into the 1960s, further growth occurred from increasing on-farm diversification. Farming entities became significant businesses in their own right. It was no longer expedient to prepare financial statements solely for fiscal requirements as the basis for stewardship, decision-useful budgetary planning, or for financing purposes (Fippard, 1957).

Initiatives were undertaken in New Zealand to foster more modern farm-management accounting practice. Better resource allocation decision-making was needed (Stone, 1968) to achieve greater productivity from emerging farm management techniques and capital intensive farming technologies. More realistic farming income determination was proposed based upon current values for budgeting (Popoff, 1974). In turn, special accounting support was required to obtain seasonal working capital financing from the major Loan and Mercantile companies, and from Bank financing for new capital developments dependent upon *'what you are worth'* (Glasgow, 1975, p. 20).

Standard accounting practice applicable to non-agricultural activities could not be relied upon to handle special agricultural accounting issues relating to joint and complementary products, climatic risks, forest fires and disease, and biological reproductive and ageing processes. *'The adoption of current values in farming accounts is essential to enable the accounts to be of real value in managerial decision making...[and] improvements in management practice and general pasture quality are enabling more farmers to make value based decisions over alternative opportunities'* (Glasgow, 1975, p. 20).

As the next sub-sections describe, leaders in the professional institutions fostered initiatives in each country during the 1970s to mid-1980s. The objective was to provide 'best practice' guidelines and standardised farm accounting terminology, classifications, systems, and financial reporting whether for the farming entity itself, the practising accountant, the farm management advisor or for agricultural economists and financiers. Sponsored committees of agricultural accounting experts were established to work co-operatively to achieve this objective.

### 3.2.1 Initiatives in Australia

A Queensland Department of Primary Industries initiative in August 1966 led to the appointment of a *Joint Committee on Standardisation of Farm Management Accounting* out of a *National Workshop on Standardisation of Terminology and Procedures in Farm Management Accounting*, held at the University of New England, Armidale, NSW, with wide representation from those associated with farm management accounting in Australia. The resulting publication was *Accounting and Farm Management* (Burns *et al.*, 1971).

Until then, the standard text-book valuation options for pastoralists' operational accounting had been to select a consistent livestock valuation accounting basis from amongst the lower of cost or market value, at average cost or at a standard rate, subject to periodic review (Yorston *et al.*, 1959, pp. 520-44).

However, by 1966, farm management accounting and administration techniques had developed for more general application for various types of Australian agriculture. Mallyon (1966) refers to grazier activities and farming produce in his *Principles and Practice of Farm Management*. These included cropping, hay, wheat, wool, skins, oats, cattle, flock and stud farming. Inflationary impacts led to increasing dis-satisfaction with special purpose historic-cost tax accounts, coupled with the need for better decision-making accounting practice with '*a view to optimising...profits*' (p. 4).

Mallyon recommended the net farm-gate price as the most realistic valuation basis for managerial decision-making for all agricultural assets and produce so as to match current income, use and cost – other than for breeding stock not intended for sale. For the latter, the valuation basis recommended was the best-assessed on-farm price, with allowance for depreciation from diminishing performance.

In the early 1970s, the Institute of Chartered Accountants in Australia (ICAA) conducted a preliminary research study, M1, to consider livestock valuation methodologies (Buckley *et al.*, 1971). Livestock was defined as '*those classes of livestock most common in Australia, such as sheep, cattle, pigs and poultry*' (para. 6). Initially the latter two classes

were eliminated from discussion *'because of their usually short economic life'* (para. 36), but in the final recommendation both pigs and poultry were included.

In 1973, the ICAA Accounting Principles Committee issued a revised M1A Research Study. It offered a *'solution to the [livestock valuation] problem which is considered to be both practical and useful; [and that] there be only one basis of accounting for all livestock, namely, current net selling value'* (Buckley *et al.*, 1973, para. 1).

Current net selling value was defined as *'the net realisable amount which the primary producer could have obtained for each category of animal at the particular balance date in any market which was then open to him, after deducting the cost of transporting to market and all other selling expenses'* (*ibid.*, para. 9).

It should be noted in passing, this definition was subject to debate during the mid-1990s when the AASB and IASC were determining relevant valuation bases. Interpretations differed as to whether produce values were at harvest, or at balance date, and whether to include (AASB), or exclude (IASC), off-farm transport-to-market and selling costs.

The Research Group discussed the influence of the average cost basis used under the provisions of the Income Tax Assessment Act and recommended instead: *'farm management accounts should be prepared for accurate measurement of profit, which will enable more soundly based decisions to be made in the operation and development of the property'* (*ibid.*, para. 13). Moreover, *'the method of accounting used should be acceptable, or capable of acceptance, for partnerships, companies, trust estates, and even income tax purposes'* (para. 15).

The study described eleven alternative cost, standard and market value measurement bases; since *'market selling value has not hitherto been an accepted basis of valuation of trading stock, except in particular circumstances'* (*ibid.*, para. 27). It concluded that current net selling value was appropriate to breeding or trading livestock and preferable to cost-based measurement bases where allocation of joint product historic costs were either notional (*e.g.* for progeny) or arbitrary (*e.g.* for meat and wool).

Current net selling value provided a *'more realistic and more easily understood measurement of profits'* (*ibid.*, para. 29) and reflected the age, weight, productivity, market and seasonal conditions prevailing during each accounting period. This specific purpose accounting basis also had wider application as *'more equitable for trusts with life tenants and remainder-men...or on change in partnership arrangements'* (para. 34); and, in other industries like merchant's 'venture' accounting.

However, current net selling value resulted in recognition of unrealised profits, unlike that from cost bases used in inventory accounting by other industrial sectors. The study recommended transfer of *'a conservative but arbitrary estimate of unrealised profits to an unrealised profits reserve pending realisation'* (*ibid.*, para. 35), for cycling to current profits when realisation occurred. This begged the question on the relevant costs for determining a reliable *quantum* of any unrealised profit.

On implementation of the new agriculture standards this issue of unrealised profit recognition re-appeared as a *cause celebre* worldwide for bearer-agricultural entities, e.g. for the listed integrated viniculture, sugar, rubber and palm oil companies.<sup>18</sup>

Neilson (1986) re-edited Mallyon (1966) to reflect the above developments. He identified ten different valuation bases, but preferred the net 'farm price' for livestock because it was objective, matched current income and cost, recognised reproductive growth, took market forces into account and was decision-useful. It also provided the economic opportunity-cost for own-use and reflected the financial consequences of decisions to sell, or not to sell livestock during the period. Neilson recognised this might result in profit recognition before realisation but *'the benefits of measuring management performance in decision making are more important than adherence to conservative accounting principles'* (1986, p. 33).

However, for stud-breeding animals, held not-for-sale, their valuation would most likely be determined periodically by an 'expert classer' with value diminishing over the breeding animal's life and performance, with allowance for depreciation as for plant and vehicles.

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<sup>18</sup> This is developed in detail below in [Section 4](#), Chapter 3 - Items 3.2 and 3.3, [Section 5](#) - Item 5.3 and in [Section 6](#).

### 3.2.2 Initiatives in New Zealand

During the 1960-80s, the research sponsor for agricultural sector accounting was The New Zealand Society of Accountants (NZSA). The NZSA commissioned experienced and specialist rural practitioners with assistance from advisers at the Agricultural University Colleges. The objective was to determine consistent accounting treatment, recommend accounting guidelines for each agricultural sector and supply 'best practice' accounting and reporting criteria for professional practitioners.

Initially the NZSA-sponsored Research Bulletins recommended more meaningful financial reporting for general and specific farming sectors. These included:-

- Research Report on Farm Accounting (NZSA, 1961);
- Farm Accounting in New Zealand (NZSA, 1966);
- Current Value Techniques in Farm Management (Toomath, 1973);
- Accounting for Price Changes (Popoff, 1974);
- Financial Reporting for Farm Estates (Smith 1974, NZSA, 1991, 3rd Edition);
- The Case for Current Values in Farm Accounts (Glasgow, 1975);
- Budgeting for Farm Management (NZSA, 1976);
- Management Accounting for the New Zealand Farmer (NZSA 1977, 1985);
- Management Accounting for Horticulture (NZSA, 1986a);
- Accounting for Forestry Activities in New Zealand (Davy, 1987); and
- Financial Reporting for Primary Producers (Clark, 1989).

The titles indicate the thrust of their research; namely, to move towards current value accounting. The objective was to reflect what the entity was worth and in the process remove historic-cost and taxation bias in farm accounting. This was consistent with what was happening in accounting more generally.

There were a number of earlier proponents. Some argued that '*in order to measure the productive and reproductive factors at any given time it is clear that market value is the only measure that can be used*' (Haisman, 1955, p. 9) and '*realism in accounting requires profit measurement and asset valuation in current terms and this in turn requires a departure from historic cost for farming entities*' (Popoff, 1974, p. 26).



The case for considering adoption of current value accounting methodologies generally was emphasised by research work conducted during the 1960s by Professor E. Stamp, then visiting Professor of Accounting at Victoria University in Wellington. Stamp argued for general adoption of current balance sheet values and recognition of income by matching 'current value of output [to] current cost of inputs' (cited, Glasgow, 1975, p. 11).

Equally influential were earlier, more general publications on the preferred applicability of current value accounting by Professor R.J. Chambers, and his colleagues at The University of Sydney (*e.g.* Chambers, 1966).

These research initiatives were reinforced from the mid-1970s onwards by rapidly escalating land, capital and livestock values. In prevailing conditions, historic-cost taxation-based livestock standard values and historic-cost asset valuations for land and farm assets became increasingly unreliable. Traditional special purpose historic-cost accounting failed to portray realistic financial and economic valuations for farming enterprises on which management planning, capital budgeting and financing could rely.

Another development was the independent *N.Z. Royal Commission of Inquiry into Inflation Accounting*, chaired by Judge Ivor Richardson (1977).<sup>19</sup> The Richardson Report illustrated the debate about the effects of historic vs. current-value accounting for forestry:

Accounts are customarily drawn up annually but in some cases profit may be recognised only after a period of years, say, at the end of the venture. Forestry is a good example. The planting and harvesting of trees extends over many years. The cash returns only become of any significance years after the start of the cash outflow. The effect of historical cost accounting is to defer the recognition of any profit until those years when the receipts start to flow in and to take no account in the balance sheet of the increase in value of the underlying assets (except for certain expenses which are capitalised) and the resulting unrealised gains. On this approach the historical accounts suggest that years of work have been profitless. The accounts make no attempt to reflect the economic viability of the enterprise. Work on one stand of timber may have produced a magnificent crop nearly ready for cutting, while the work on another stand may have resulted in more or less complete failure. Under historical cost accounting both stands will be treated the same unless the inferior stand is so bad that its market value is lower than its historical cost. The point is that the significance of the business operations lies in the asset values, not in the cash flow. Accordingly, historical cost accounts cannot satisfactorily measure the performance of the enterprise or provide for the assessment of its future prospects (Richardson, 1977, para. 8.4).

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<sup>19</sup> This Inquiry was preceded by the Sandilands Committee *Report on Inflation Accounting* in the United Kingdom in 1975.

Local research activities on agricultural accounting issues culminated in publication of three major Agricultural Practice Bulletins for general application and for specific sectors prepared under sponsorship of:

- the NZSA's Farm Accounting sub-committee *Management Accounting for the New Zealand Farmer – R-404* prepared in May 1977, and subsequently updated in October 1985 (NZSA, 1985);
- the Horticultural sub-committee of the Accounting Research and Standards Board Farm Accounting Committee *Management Accounting for Horticulture – R-406* (NZSA, 1986a); and
- Peat Marwick for the Auditing Committee of the Accounting Research and Standards Board *Forestry Accounting in New Zealand*, which in turn developed into *Accounting for Forestry Activities in New Zealand - R-117* (Davy, 1987).

The NZSA Farm Accounting sub-committee referred with approval in the inaugural *R-404 Bulletin* to the earlier work of the Queensland Joint Committee on Standardisation of Farm Management Accounting and, in particular, acknowledged extracts from their report *Accounting and Planning for Farm Management* (Burns *et al.*, 1971).

The *R-406 Research Bulletin* resulted from the rapid farming diversifications from traditional apple, hops and tobacco crops into new horticultural ventures which required accounting guidelines relevant for newly commercialised orchard crops such as grapes, kiwi-fruit, pip- and berry-fruits, and other exotic fruits.

At that time, the *R-117 Forestry Research Bulletin* lay outside the scope of general agricultural sector deliberations. However it is necessary to include forestry in this existing practice discussion because of the pivotal role the sector was to play in formulating the new *SGARA* standard in Australia.

### **3.3 Absence of General Purpose Financial Accounting for Agriculture**

Why then were there no formal general purpose accounting standards in New Zealand, Australia, or for agricultural activities worldwide? Agriculture was the most important economic sector in New Zealand and, to a lesser extent, in Australia.

Apart from forestry, until the mid-1990s preparers or users of agricultural sector financial statements perceived no need for an approved general standard to cater for biological reproduction and growth. One reason was the lack of non-forestry, publicly-listed agricultural reporting entities in New Zealand. There was only one listed viniculture company, Montana Ltd. In Australia there were comparatively few listed entities, albeit many were large with long-standing pedigrees; *e.g.* Australian Agricultural Company Ltd., BRL Hardy Ltd., CSR Ltd., North Broken Hill Peko Ltd. and Southcorp Ltd. Some of these companies (*e.g.* the latter three) operated in other industrial sectors than agriculture.

Lack of demand for guidance in this area possibly reflected the reality that agriculture was too broad a topic with too many differing sectors to mould into a single industry standard. Instead, the profession in Australia and NZSA concentrated on developing ‘best practice’ guidelines and technical aids for consistent sector accounting and reporting by the profession alongside, but outside, mainstream standards.

Another possibility was lack of an appropriate taxonomy defining agriculture. It was regarded as more relevant for preparers and users to focus on individual sectors. Thus no attempt was made to develop an omnibus Agriculture standard for general purpose financial reporting. Perhaps professionals recognised the irreconcilable ‘consumable *vs.* bearer’ economic functional dichotomy - unless a standard was prepared for each.

Furthermore, additional to no identified need, existing authorised accounting standards for each of the accounting standards for *Revenue*; *Inventories*; *Leases*; and for *Property, Plant and Equipment*<sup>20</sup> expressly excluded biological assets related to agricultural activity.

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<sup>20</sup> The precursors to IAS 2 *Inventories*; IAS 16 *Property, Plant and Equipment*; IAS 17 *Leases*; and IAS 18 *Revenue*.

Given that policy vacuum, reliance had been placed in New Zealand upon sector specific guidelines covering recommended accounting treatment and reporting for *Livestock - TPA-5* (ARSB, 1986); *Bloodstock - TPA-7* (ARSB, 1988) and *Horticulture* (NZSA, 1986a); and, embryonically, the Research Bulletin - *R-117 Forestry* (Davy, 1987).

Furthermore, in New Zealand the newly-legislated Financial Reporting Act, 1993 (FRA) established the framework for reporting of financial statements by public- and private-sector entities. Previously these ‘rules’ were contained in the 1933 and 1955 Companies Acts, with particular emphasis on the ‘true and fair view’ reporting criterion.

The FRA authorised the reconstituted Accounting Standards Review Board (ASRB-NZ) to determine generally accepted accounting practice (NZ-GAAP) carrying authoritative support for financial reporting in New Zealand. The FRA removed the previous true and fair value override by legislating mandatory adherence to the financial reporting under NZ-GAAP established and authorised by the ASRB-NZ. This now represented a statutory true and fair view.<sup>21</sup>

In the absence of approved local accounting standards, regard was had either to guidelines issued by an overseas professional body, for example from Australia, the U.S.A. or Canada, or, to Guidance Bulletins and TPAs issued in New Zealand for specific sectors - all carried the *imprimatur* of generally accepted accounting practice. Since none was mandatory, there was scope to ‘cherry-pick’ a relevant standard or guideline.

This situation was not unique to Australia and New Zealand. When the IASC eventually established its Agriculture Steering Committee (SC) in 1995 to consider a specific standard for *Agriculture*, the SC undertook a worldwide inventory of:

- exclusions in existing standards relating to agricultural activities, summarised in Appendix 1; and with
- current accounting guidelines and sector practices recorded in Appendix 2.

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<sup>21</sup> Financial Reporting Act, 1993, Sections 3-8. However, where directors consider financial statements do not give a true and fair view they must add such information and explanations to provide a true and fair view, but without altering the financial statements, and the auditor should then opine on the directors’ assessment.

The IASC summary covered guidelines for specific sectors rather than any identified approved omnibus reporting basis: for example

- General accounting for farming and types of Agricultural producer or collective entities - Australia, Canada, India, New Zealand, South Africa, United States;
- Livestock & Bloodstock – Australia, New Zealand, South Africa;
- Dairy Farming – Thailand;
- Forestry - Chile, New Zealand, United Nations;
- Plantations – India, Malaysia, Papua New Guinea, Sri Lanka;
- Poultry Farming – India, New Zealand;
- Horticulture – New Zealand;
- Aquaculture – Malaysia;
- Special Research Topics:
  - Current value techniques in Farm Accounting – New Zealand;
  - Accounting for Self-Generating and Regenerating Assets - Australia.

In the absence of approved formal standards and prior to the new IAS-41 *Agriculture* standard becoming mandatory in New Zealand, on or after 1 January 2007, the alternative for public issuers, and their auditors, was to adapt existing standards for inventory and asset valuations. These were consistent with all other non-agricultural accounting policies - even if technically precluded for agricultural activities by respective standards.

When the Australian *SGARA* standard was issued in August 1998, it became an approved accounting basis for New Zealand reporting entities. However, because of initial concerns by the few listed agricultural entities about implications of that standard, each continued with previous local reporting practice. The only known exception was Carter Holt Harvey Ltd. It had a dual listing in New Zealand and Australia, with ASX-listing obligation to respond to the AASB 1037 *SGARA* reporting standard from the 1 July 2000 operative date.

### **3.4 Approved Guidelines and Sector Technical Guidance in New Zealand**

The NZSA produced various sector Research Bulletins and Management Accounting Guidelines. These formed part of NZ-GAAP but were not always adopted in practice either partially or in full, as there were alternative accounting treatments available with ‘authoritative support’ within the ASRB-NZ reporting framework (NZSA, 1993, para. 4).

#### ***3.4.1 Technical Practice Aids***

The first, *Technical Practice Aid No.5 ‘Livestock’*, was issued by the NZSA Accounting Research and Standards Board in 1986 (ARSB, 1986). It represented a return to first principles for accounting for trading or consumable livestock with no apparent recognition of the earlier ICAA M1A Research Study (Buckley *et al.*, 1973).

TPA-5 defined *‘livestock as animals farmed or dealt in for profit’*. In summary, it recommended departure from the standard-value inventory basis for livestock valuation. Arguably, the latter had *‘the merit of simplicity, but little else’* (ARSB, 1986, paras. 8-11).

TPA-5 recommended net current value - represented by open market current realisations, less reasonably anticipated disposal costs, as providing the most useful information for management and investor decision-making (para. 12). There were ample sources of price reference data from weekly stock sales throughout the country and *‘the fluctuations in the value...and the relative gains/losses are integral to the understanding and management of the business’* (para. 14).

Any unrealised holding gains or losses derived from changes in livestock numbers or changes between age-classes were to be included as a component of operating profit (para. 15). But unrealised holding gains/losses from changes in livestock net current values were to be recognised separately in the income statement, after net operating income (para. 16).

TPA-5 was followed by TPA-7 *Accounting for Bloodstock Enterprises* (ARSB, 1988).

TPA-7 defined Bloodstock as referring to both thoroughbred and standard-bred horses. A Bloodstock Enterprise was defined as engaged in commercial breeding and/or racing of bloodstock.<sup>22</sup> For consistency, practitioners applied the same principles to stud cattle, sheep, stags and hinds.

TPA-7 recommended accounting for this class of 'bearer' livestock as follows:

- normal inventory accounting principles, being lower of cost or net market value, for both bloodstock held-for-sale and progeny, because the latter current values were likely to be uncertain and '*seriously distort the balance sheet and profit and loss statements*' (*ibid.*, paras. 4.1 a) + b)); however
- stallion or brood mare assets were in the nature of fixed assets, '*held for the production of income rather than increases in value*' to be recorded at cost, preferably modified historic cost, with any holding gains or periodic revaluations held in reserves '*since strict application of valuation at historic cost may result in serious understatement of the asset base of the enterprise*' (para. 4.1 c)), and with
- depreciation to be determined in accordance with normal depreciation rules.

### **3.4.2 New Zealand Technical Guidance for Other Agricultural Sectors**

#### **3.4.2.1. Horticulture**

The ASRB was busy in 1986. In addition to TPA-5, and as part of continuing guidance on accounting for farming activities, the ARSB's Horticulture sub-committee also published its R-406 Bulletin, *Management Accounting for Horticulture* (NZSA, 1986a). The preface indicated there were few precedents available world-wide. R-406 therefore sought to provide support for this increasingly important local agricultural sector with emphasis on the reporting of financial information for decision-making rather than production of accounting income for income tax calculations.

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<sup>22</sup> N.B. Both AASB 1037 and IAS 41, by definition, specifically excluded horses held for racing; because they were not held or managed for biological purposes.

The R-406 Bulletin distinguished horticultural taxonomy classifications as:

- commercial crops: being *consumable* cash-type crops which were regarded as annual produce not the subject of the R-406 technical guidance; and
- '*perennial trees, bushes, vines and plants typically having a development and maintenance investment period followed by a production period...where the parent plant continues growing after each annual crop harvest*'. These latter were described generically as '*plants for simplicity to denote trees, bushes, vines and plants growing any of the above [commercial] crops*' (NZSA, 1986a, p. 4).

These two *crops* and *plants* categories were later termed 'consumable SGARAs' and 'bearer SGARAs' in DP 23 (Roberts *et al.*, 1995).

R-406 described the rationale for capitalisation of annual value increments, with revaluation credited to reserves at current values and for the subsequent useful-life depreciation of these perennial plants, since:

horticulture plants are considered to meet the criteria for classification as a fixed asset and are, therefore, subject to depreciation, thus meeting the Society's definition of a 'depreciable asset' (NZSA, 1984) ... because it is an asset which:

- is expected to be used during one or more accounting periods;
- has a limited useful life; and
- is held...for use in the production or supply...of goods (NZSA, 1986a, p. 39).

Further reasons were adduced because of conformity to the 'matching concept' whereby '*expenditures which are expected with reasonable certainty to produce future identifiable benefits sufficient to cover the amount deferred may be allocated to future accounting periods*' (NZSA, 1979, p. 39).

This conceptual position relied on precedent from the American *Statement of Position Accounting for Agricultural Producers and Agricultural Co-operatives* (AICPA, 1985):

limited-life development costs and direct and indirect development costs of orchards, groves, vineyards and intermediate-life plants should be capitalised during the development period and depreciated over the estimated useful life of the land development or that of the tree, vine or plant (citing 85.3 para. .067, NZSA, 1986a).



The R-406 guidance concluded, after taking everything into account, that:

costs incurred in the development years of a crop should be capitalised followed by later depreciation...with each category of land, shelter and plants capitalised and disclosed individually as discrete asset classes separately depreciated over respective useful asset lives on a straight line basis (NZSA, 1986a, pp. 40-1).

Inventory valuation warranted special analysis. In certain circumstances the traditional SSAP-4 *Accounting for Inventories* (NZSA, 1986b) was considered appropriate, namely the lower of cost and net realisable value, but this may be qualified since, '*with crops there is often a difficulty in obtaining appropriate costs which makes it difficult to apply that criterion*' or it is not considered useful to users. For example,

*Accounting Research Study 13* (Barden, 1973), commented that:

exceptional cases exist in which it is not practicable to determine an appropriate cost base for products. A market base is acceptable if the products have:

- a) an immediate marketability at quoted market prices that cannot be influenced by the producer;
- b) characteristics of unit inter-changeability; and
- c) relatively insignificant costs of disposal (NZSA, 1986a, p. 47).

The use of a market base in certain circumstances as an acceptable alternative to cost was identified with approval in the AICPA *Statement of Position*:

an agricultural producer should report inventories of harvested crops held for sale at:

- a) the lower of cost or market, or
- b) in accordance with established industry practices, at sales price less estimated costs of disposals, when the following conditions exist:
  - the product has a reliable, readily determinable and realisable market price,
  - the product has relatively insignificant and predictable costs of disposal,
  - the product is available for immediate delivery (AICPA, 1985, para. 039).

As a result, the sub-committee concluded '*valuation of horticultural inventories is dependent upon whether or not there is an established or reliable market price*'. Valuation could be at cost or at market value. If costs were difficult to ascertain, and there was an established price net of estimated disposal costs, then net market value was acceptable. If there were no established market price, then inventories should be valued at the lower of cost or net realisable value (NZSA, 1986a, p. 47).

### 3.4.2.2. Financial Reporting for Primary Producers

In 1989, the NZSA Primary Sector Accounting sub-committee published *Financial Reporting for Primary Producers* (Clark, 1989). This complemented and was an extension to R-404 (NZSA, 1985) but concentrated upon recommended financial reporting treatments because of continuing changes in financial reporting requirements.

The purpose of the publication was ‘*to consider what should constitute generally accepted accounting practice for primary producers with a view to providing guidance on GPFR and valuation policies and techniques for primary producers and for their financial advisers*’ (Clark, 1989, p. 1). Primary producer activities covered the full gamut of agricultural sectors from livestock through to fish and marine farming – with the notable exception of forestry.

The objective was to set out the principles for sector financial reporting to present:

the producer’s economic position in a meaningful fashion...[as] essential for ability to make sound financial decisions...and to assess with a greater degree of precision the performance of their operations for the year and the financial condition of the business at a specified date (*ibid.*, p. 2).

The sub-committee supplied guidelines to help establish the amount of operating profit determined at current values and the valuation of assets at ‘*some form of current value [to provide] a more realistic measure of the resources actually available to the producer*’ (*ibid.*, p. 7).

Thus, the sub-committee provided ‘best practice’ recommendations for:

- **Livestock:** the principles contained in TPA-5 were endorsed for livestock valuation at net current value because ‘*this method provides the most realistic and useful information for the users of financial statements*’ - with one exception, namely, in the calculation and treatment of holding gains and losses (*ibid.*, pp. 11-12).

TPA-5 provided the methodology to isolate these into their separate livestock numbers and value change components. Any gains/losses in livestock numbers were included in the calculation of net operating profit/loss, whilst changes due to market price fluctuations were transferred to reserves as an adjustment to owner’s equity;

- **High-Priced Livestock:** These were identified as a separate class because of breeding potential. Each animal should be separately identified, as though for fixed assets, and subject to modified historic cost by periodic revaluations, as transfers to/from reserves, with each depreciated over its estimated useful life following the principles expressed in TPA-7 (*ibid.*, pp. 12-13);
- **Horticulture:** The sub-committee recommended financial accounting and reporting for 'long term crops' for horticulture; that is, for trees, bushes, vines and perennial crops which are developed and maintained for production and whose useful life extends beyond one year. In summary, it endorsed R-406. These assets were considered to meet the classification of a depreciable asset, as defined in SSAP-3 *Accounting for Depreciation* (NZSA, 1984).

Establishment costs were accumulated and capitalised during development until commercial maturity commenced, whereupon useful-life depreciation was calculated on a units-of-production or straight-line basis over the expected useful economic life of that horticultural asset, with all other maintenance and operating costs expensed.

The sub-committee distinguished between land, including permanent improvements to land, and limited-life improvements which increase the productive capacity of the land. The latter included water wells and irrigation systems, fencing and trellising. Each was depreciated to cost-of-production as a charge against income. The sub-committee recommended these assets be revalued periodically and holding gains credited to revaluation reserves since '*it is desirable to record assets at current values in order to portray the present equity of owners*' (*ibid.*, p. 22);

- **Inventories:** The sub-committee traversed the precedents established by the AICPA (1985), noting too that the Canadian Institute of Chartered Accountants (1986) concurred with that view.

The sub-committee maintained there was no justification for:

the lower of cost or market rule except under the principle of conservatism...[instead] use of the net realisable value method...provides a more contemporary figure on the balance sheet...and is much easier to implement than the lower of cost or market for some categories of inventory (Clark, 1989, p. 16).

The above asset and valuation procedures remained standard practice pre-adoption of NZ-IFRS. Much of the above was contained in the IASC's DSOP, possibly influenced by the appointment in 1995 of two New Zealanders for the formative stages of the IASC's *Agriculture* steering committee (SC) deliberations. One of them, Ms B.A. Monopoli, was an inaugural member and remained on the SC's for its full term to December 2000.

### **Prevailing Accounting Australasian Practice for Horticulture Bearer Assets**

The general principles for horticulture outlined above were in common use in Australia, prior to SGARA-introduction in 2000/2001, and in New Zealand prior to June 2008<sup>23</sup>, but with some differences in detail.

Practice is summarised under key elements:

- *harvested produce for sale*: recorded at net realisable value;
- *harvested produce for inventory*: recorded at lower of cost or market value;
- *development expenditure*: all development costs capitalised and recorded as capital work in progress, with capitalisation continuing until the horticultural asset was considered available for commercial production. Pre-SGARA examples included capitalisation for three years (BRL-Hardy, 1999-2001); four years (Southcorp, 2000-2003); or an unstated period (Tandou, 2002).

For *almond trees*: all costs were accumulated for the first three years of orchard development; once immature trees commenced bearing a commercial crop, a progressive proportion of annual growing costs was expensed on the basis of expected yield-to-full-maturity which was deemed to occur in the eighth year (Select, 2001);

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<sup>23</sup> This was the last possible date for adopting NZ-IFRS.

- *asset carrying value:* horticultural improvements were revalued periodically, generally based on fair market value for existing use. Typically valuations were reviewed annually as directors' valuations, supported by triennial reference to an independent valuer. Valuations were conducted for, *e.g.* a vineyard, as a single asset class, or segregated into respective vines and land asset class components. The net market value of vines as an asset class was calculated as the difference between the net present value of net cash flows expected to be generated by the vines and the net market value of the land on which the vines were growing. Assumptions were made for future market prices expected from the latest vintage and growth of the vines. These accounting policies were applied pre-SGARA, *e.g.* by BRL-Hardy Ltd., Foster's Ltd. and Pipers Brook Ltd.

Revaluation increments/decrements were credited directly to revaluation reserve in equity, unless the decrement exceeded the previous 'asset class' carrying value, in which case the net decrement was expensed in the profit and loss account;

- *depreciation:* this was typically determined on a straight-line basis over the asset's expected useful horticultural life. Vine lives varied from 20-50 years (BRL-Hardy, 1999-2001) and 15-30 years (Southcorp, 2000-2003). New Zealand Wine Company initially depreciated vines over 25 years but amended this to a '*deemed more realistic*' 50 years in 2005 (NZWC, 2005); whereas Palliser Estate made no depreciation provision for vines or vine support structures. Instead, replacements of vine support structures and vines were expensed as a cost of production in the year incurred (Palliser, 2000).

### 3.5 Forestry Accounting Practice in New Zealand

This was another sector where significant variation in accounting practice was prevalent. In order to achieve some consistency, efforts were made to achieve a common valuation basis through the auspices of the NZSA in R-117 *Accounting for Forestry Activities in New Zealand* (Davy, 1987).

R-117 summarised some unique problems for *pinus radiata* forestry accounting:

- a 25-30 year growth period with costs predominantly incurred in the early years, with revenue realisation during a relatively short period at maturity many years later;
- forest growth appreciated in value from seedling to fully grown tree at maturity;
- during the long growth period factors may change which can influence reporting, such as new silviculture research, different silvicultural management regimes, changes in targeted end-use; and
- costs incurred historically did not reflect end-value within a forest; for instance, high development costs did not necessarily equate to high value, and *vice versa*, and cost inflation was not taken into account for comparative purposes (*ibid.*, p. 7).

For these reasons forestry accounting practice had special features and presented problematic issues for historic cost reporting without formal accounting guidelines. Since there were none, differing accounting practices evolved.

Preceding publication of R-117, there were two principal valuation methods in general use, with variations, by the major New Zealand listed forestry entities, with some using both depending in circumstances:

- *the stand/unit costing or cost-of-bush method:*  
all direct and indirect costs were capitalised to individual forest blocks, or age-class stands, pending harvest. On felling, accumulated historic costs by stands were allocated against current revenue.

In effect, this was a quasi-cropping regime (*ibid.*, p. 9), *e. g.* as adopted by Alex Harvey Ltd., Carter Holt Ltd., Fletcher Challenge Ltd., The New Zealand Forest Service, and Odilins Ltd.; or

- *the perpetual/sustained yield method:*

the forest was assumed to continue in perpetuity so that until the first harvest rotation, or when a sustained yield was achieved, all development costs were capitalised and thereafter all current annual costs were expensed against current annual harvest revenues – in principle, this reflected a continuing forestry resource with a presumed constant silvicultural regime without annual over- or under-cutting (*ibid.*, pp. 10-11) – e.g. variously adopted for some of their forests by New Zealand Forest Products Ltd., Fletcher Challenge Ltd., and Evergreen Forests Ltd.

Each had advantages and disadvantages. However, neither was satisfactory on a continuing basis. For the former, capitalised costs and therefore asset values, and resultant net equity, diverged from realisable value; whilst for the latter, the assumptions became impractical over time. Moreover, different practices applied to associated forestry-related expenditures. Some companies charged interest on borrowings annually to expenses on general or specific borrowings whilst others capitalised general or specific interest costs.

Deferred tax liabilities were not always charged against forestry revaluations. Some followed these principles or variants, others did not. These were further complicated by the variety of special fiscal subsidies, grants and allowances. In 1985, Government phased out immediate income tax deductibility of all forestry expenditures against current income. The change in tax rules favoured the ‘cost-of-bush’ accounting treatment. But, given the potentially long periods to harvest, there were questions about the conceptual applicability of deferred tax credits on net expenditures, which may or may not have been claimed already and could only crystallise with any certainty many years into the future.

In 1984, to try and resolve these matters, Waikato University convened a working party of major forestry representatives along with others with an interest in forestry accounting.

The resulting report (Waikato, 1985) was concerned with the unsatisfactory diversity in reporting practice particularly ‘*because it does not reflect any logical and consistent conceptual basis for measuring capital and income*’ (p. 24). Furthermore, ‘*for consistent reporting there will need to be a consensus both within the forestry industry and among accountants as to the appropriate accounting policies to be applied*’ (p. 6).

The Waikato Working Party Report included the following principal recommendations:

- forest assets should, in principle, be valued at current market value – that is, the current cost to acquire tree crops, including land where relevant, of similar age, species, conditions, topography and location; with
- any change in forest value in a year representing a gain or loss in that year; and
- under this concept, both the revenue from the produce harvested and the gain or loss in the value of the forest would be taken to the income statement, and be offset against expenses incurred in the year on forestry activities (*ibid.*, p. 24).

The report outlined the balance sheet recognition issues arising from revaluing forest assets. The revaluation may be credited direct to a revaluation reserve; or, to the profit and loss account - but then transferred to an unrealised revaluation reserve for later cycling so revaluation gains would not be recognised as available for current dividend distributions prior to realisation. In either case; the accounting treatment used should be fully disclosed.

The conceptual basis for crediting revaluations to profit and loss was that all changes in an entity's wealth were recognised annually. These changes may arise from natural growth and re-plantings; reductions in total forest volume from clear-felling, or by natural disaster; and from real changes in end-market value of lumber; or in monetary-value due to inflation.

However, it was also recognised that whilst real growth and inventory changes should be recorded in the profit and loss account, any monetary capital maintenance effects should preferably be reflected, where possible, in capital reserves within equity, even though it may be difficult to separate the monetary price change component accurately.

As the forest stand was felled, income would be credited to sales; but the value of the growth of the trees may already have been recognised in profit and loss as unrealised gains throughout the 'life' of the stand. To avoid double inventory-accounting of profits, an offset was required to record the depletion of the forest-tree asset revaluation as a cost-of-goods sold adjustment. In effect, '*the forest asset is treated like inventory*' (*ibid.*, p. 25).

This is the first reference found to an 'inventory concept' for trees in a forest stand.



R-117 described policy-setting criteria and identified unresolved issues for future forestry accounting guidelines, or for a new forestry standard. These included whether:

- current forest valuations should be recorded in the balance sheet;
- resulting revaluation changes should be reported either as a direct credit to a revaluation reserve or a credit within the profit and loss account;
- accounting should be on a unit-stand or perpetual-forest basis;
- interest and continuing silvicultural costs should be capitalised on forest development expenditures with credits to a forest revaluation reserve through profit or loss; with any assessed net current value increment/decrement differences identified and expensed in the profit and loss account; and whether
- a capital maintenance charge should be an offset against unrealised revaluation value gains in order to determine volume and valuation increments.

Regardless, a major recommendation related to improved disclosures about forest valuations (*ibid.*, pp. 33-4); including:

- description of the valuation adopted, the method and discount rate;
- if interest were capitalised, then the fact and amount should be disclosed;
- where changes in valuation were charged to profit and loss, disclosure should distinguish between realised revenue from felling and unrealised change in valuation;
- where a revaluation were credited to revaluation reserve then the basis for releasing that reserve should be disclosed;
- forests and associated land should be separately classified in the balance sheet with Notes disclosures on the forest age-profile, and its value by age-classes; and
- asset revaluations should take into account all deferred tax liabilities together with the deferred tax effect on capitalised interest already claimed for income tax deduction.

R-117 reflected the diversity of existing accounting policies with each debatable and no consensus found on a consistent forestry accounting valuation or a reporting 'best practice' guideline. There was a specific accounting problem to be solved.

### 3.5.1 Major Changes Proposed for Forestry Accounting and Reporting

As if to reinforce the debate, in 1985 the two leading forestry companies, New Zealand Forest Products Ltd. (NZFP) and Fletcher Challenge Ltd. (FCL) announced significant proposed changes in respective forest valuation policies and methodologies. Each adopted entirely different valuation proposals.

The NZFP 1986 forest accounting policy specified:

#### FOREST - INCLUDING LAND

Development forests are recorded at replacement cost at 31 March 1985 increased by subsequent expenditure including holding costs.

Production forests are recorded at estimated market value at 31 March 1985 adjusted for costs attributable to subsequent forest volume variations and holding costs. The annual costs of maintenance, protection and management attributable to the volume of wood extracted are treated as revenue expenditure and included in the cost of wood supplied to the mills each year.

Forest land is recorded at market value determined by independent valuation at 31 March 1985 adjusted for subsequent acquisitions and disposals. Permanent roads are valued at cost.

The value of the forest asset is reviewed periodically and changes are taken to the appropriate revaluation reserves.

The changes in accounting policy include:

- holding costs relating to the financing of development forest being compounded and those relating to forestry land being capitalised;
- annual holding costs, maintenance, protection and management costs incurred on production forests being adjusted to reflect the portion attributable to the change in wood volume in the forest (Waikato, 1985, *op. cit.*, pp. 18-19).

This marked a major departure from NZFP's former 'sustainable forestry' regime with various internal cost adjustments charged between operating expenses and forest assets.

By way of further contrast, R-117 supplied an extract from the announced FCL proposal to adopt a management market-smoothing-value basis for forest accounting:

the quantified incremental growth of the forests will be recognised in the accounts as it occurs based on the present market value of the forest which reflects the current market value for the likely end use of the forest units.

The changes in the economic value of the forest will be included in earnings.

The net present value equates with the economic value of a forest because of the ability of forest values to ride out cyclical downturns and cycles in economic activity (*ibid*, p. 19).

Closer examination of Fletcher Challenge Ltd's 1986 announcement is warranted because of what subsequently occurred. The expectation was that the move from the

'unit stand' cost basis to 'net current value' would be value accretive at a time FCL was in an aggressive growth phase to become New Zealand's first Fortune-500 company.

FCL's 'unit stand' cost method had previously capitalised all development and ongoing maintenance costs until harvest including, in FCL's case, forest interest funding-costs calculated as interest costs on total funds employed. With the long period to maturity, this compounding cost capitalisation could result in a higher book value than market value (NZSA, 1986c). However Fletcher Challenge Forests Ltd. (FCF, FCL's principal forestry subsidiary) later confirmed capitalisation would be adjusted so that capitalised cost did not exceed management's estimated recoverable amount.

FCL proposed to determine net present values (NPVs) derived from market values based upon management's expectation of likely end-use, with future uncommitted wood volumes being valued '*at its most optimum use*' (NZSA, 1986c, p. 9). Forestry expenditure would be expensed, not capitalised, as a cost of obtaining future incremental volume growth. The NPV calculation included all future costs discounted back from the expected realisation maturity date to obtain a satisfactory return on the forest. The initial proposed discount rate was 7% - but this was later amended to 8% which '*equated to the economic value of a forest because of the ability to ride out cyclical downturns and cycles in economic activity*' (FCF, 2001-2003) In effect, this provided an income-smoothed measurement method based upon management's chosen discount rate for its assessed uncommitted optimum forest end-use.

FCL summarised the advantages as:

- earnings will include all increases and decreases in economic value resulting from the period of investment;
- reported earnings will allow a more effective assessment of the returns on cash resources employed on forest growing activities; and
- earnings become the growth as it occurs set against the cost of obtaining that growth (NZSA, 1986c, p. 9).

This was a first in New Zealand. However, implementation of FCL's new NPV policy was deferred pending implementation of the AASB 1037 *SGARA* standard and the confirmation of the IASC's proposed IAS 41 *Agriculture* standard issued in December 2000.

In its June 2001 Annual Report, the Fletcher Challenge Forests Ltd. (FCF) business segment described the change in accounting policy whereby:

the forest crop asset is revalued to the Directors' estimate of market valuation; changes in valuation [are included] within earnings before taxation in the Statement of Financial Performance. This resulted in a pre-tax devaluation of the forest crop of NZ\$625 million. The change of policy was to provide timely, relevant and transparent forest valuation information which is consistent with the Australian AASB 1037 Standard and the IAS 41 Standard.

Age-class market valuations were assessed (Note 1ii)

Age-class 1-5 years: compounded replacement cost (CRC);

Age-class 6-14 years: progressive weighting of CRC from year 6 to an NPV of future net cash flows at end of year 14;

Age-class 15 years+: NPV of future cash flows (FCF, 2001-2003).

The change in policy was implemented at a time when the NZ\$ exchange rate was appreciating coupled with declining world US\$-based prices for logs, timber and timber products. The impairment consequences were dramatic.

FCF's forestry carrying value and movements are recorded in Table 3 below. Prior to the change of policy on 30 June 2001, the FCF Plantation Crop was reported at a capitalised cost valuation of NZ\$1.65 billion.

Three years later the carrying value was NZ\$582mn. This was due to the subsequent valuation adjustments and impairment write-downs associated with implementing FCL's new accounting policy which reflected the new AASB 1037 and IAS 41 'fair value' methodology.

**Table 3. FLETCHER CHALLENGE FORESTS LIMITED**

Unit - NZ\$ millions	2000	2001	2002	2003
<b>Notes to Financial Report</b>		<b>20</b>	<b>16</b>	<b>17 + 30</b>
Weighted Average Discount Rate (Note 1)		8.0%	8.0%	9.75%
Opening Forest Crop at Valuation	1411	1648	1123	1176
Cutting Rights Sale				[143]
Net Opening Value	1411	1648	1123	1033
Capitalised Operating costs & Interest	108	111		
Forest Costs capitalised	21	18		
Growth & Replanting			128	120
Depletion - harvesting removals	[90]	[86]	[77]	[106]
Change in Log Prices			18	[298]
Permanent Impairment (Note 2)		[207]		
Revaluation (Note 3)		[625]		
Change in Discount Rate (Note 1)				[145]
Currency Translation	198	264		
Other			[16]	[22]
Closing Forest Crop Carrying Valuation	1648	1123	1176	582
Net Transfer to Earnings		[525]	53	[451]

Source: Fletcher Challenge Forests Ltd. Annual Reports 2001-2003.

*Note 1.* Net present value of future cash flows of harvesting and marketing wood discounted rate after tax @ 7.5% (2003: 10.5%);

Replacement costs compounded at 5% to give a weighted average real after tax discounting rate of 8% (2003: 9.75%).

*Note 2.* Low log costs where carrying value in excess of estimated recoverable amount of crop. Recoverable amount of expected future discounted net cash flows taking into account age, condition, location and intended use of plantation forest crop.

*Note 3.* Effect of change in accounting policy from historic cost to market value prices.

Fletcher Challenge Limited was listed on the New Zealand, Australian and New York stock exchanges. FCL was therefore required to reconcile the differing NZ-GAAP and US-GAAP forestry valuations under prevailing accounting standards.

Tables 4 and 5 below provide a unique early comparison to illustrate the effects on earnings and carrying values between FCL's new AASB 1037 and proposed IAS 41-based NZ-GAAP accounting policy with the historical-cost method consistent with US-GAAP.

Under US-GAAP the carrying value of the Tahorakauri and Tauhara forests was \$69 million higher as a consequence of cumulative US-GAAP differences resulting in additional write down on sale. The historic cost carrying value under US-GAAP resulted in a permanent impairment difference of \$536 million in June 2003 and \$118 million in June 2002 when compared to recoverable amount. The permanent impairments were identified by using undiscounted cash flows as required under US-GAAP. The impairment in June 2003 – see the summary table below - primarily arose due to a change in market conditions as a result of using an average of the previous 12-quarter [trailing] price series. This was consistent with the Group's market value methodology compared to the former use for impairment test purposes of the 25<sup>th</sup> percentile of a long term historical price series (FCF, 2001-2003).

**Table 4. FLETCHER CHALLENGE FORESTS LTD. - US-GAAP Adjustments**

Unit - NZ\$ Millions	2001	2002	2003
<b>Notes to the Accounts – Reference Nos.</b>	<b>34</b>	<b>30</b>	<b>30</b>
Reverse Current Period Revaluation	625	[53]	451
Capitalise Silvi-cultural Costs	-	21	22
Current Period Depletions based on US-GAAP Historical Cost	-	[82]	[106]
Capitalise Funding Costs	-	22	18
Loss on Sale of Forests cutting rights	-	-	[69]
Permanent Impairments on US-GAAP Historic Cost Value	-	[118]	[536]
Pre-Tax US-GAAP Earnings Adjustment	<b>625</b>	<b>[210]</b>	<b>[220]</b>

Source: Fletcher Challenge Forests Ltd. Annual Report 2001-2003.

A further measure of these differing accounting treatments is revealed in Table 5 for the reconciliation of the NZ-GAAP market valuation methodology to the US-GAAP historical cost basis (FCF, 2001-2003). In 2001, the difference increased FCF's US-GAAP earnings by approx. NZ\$2.7bn., but by 2003 the reduction was NZ\$152mn.

**Table 5. FLETCHER CHALLENGE FORESTS LTD. - US-GAAP Reconciliation**

NZ\$ Millions	2001	2002	2003
<b>Net Earnings After Tax – NZ-GAAP</b>	<b>[1377]</b>	<b>[249]</b>	<b>[271]</b>
<b>US-GAAP Adjustments</b>			
Continuing Operations			
Revaluation of Forest Crop	555	[138]	[149]
Others	70	[3]	[3]
Total Continuing Operations	<b>[752]</b>	<b>[390]</b>	<b>[423]</b>
Discontinued Operations	2071	-	-
<b>Post-Tax Net Earnings with US-GAAP</b>	<b>1319</b>	<b>[390]</b>	<b>[423]</b>

Source: Fletcher Challenge Forests Ltd. Annual Report, 2003.

In 2003, just prior to balance date, the FCL Parent Company announced FCF would be restructured with its forest estate sold before the 30 June financial year end. The renamed successor company, Tenon Ltd., eventually sold all remaining forestry assets.

Tenon Ltd. recorded further write downs in an historical comparative schedule for 'Discontinued Operations' (Note 32, Tenon, 2004). The losses were compounded for separate forest plantation assets held elsewhere in the consolidated Fletcher Challenge Group. The aggregate losses were revealed a year later at NZ\$1.8 billion, partly attributable to forest assets held by FCL itself, but also to the write down in value of one of its Forest Partnerships previously sold to third party investors after the Partnership breached its banking covenants and was placed in liquidation (FCL, 2004).

### **3.5.2 Accounting Policies for Other Listed Forestry Entities.**

By contrast, the forestry accounting policies adopted by Opio Forestry Fund and Evergreen Forests Limited illustrated the respective traditional unit-stand capitalisation and perpetual sustainable yield alternatives.

#### **Opio Forestry Fund (also for Nuhaka Forestry Fund, and Odilins Forests Ltd.)**

Land and forest investments: Land and forest investments, including cost of developing forests, are initially recorded at historic cost, and then revalued to net current value every six months. Unrealised gains or losses are reflected as movements in the Fund revaluation reserve.

Operating costs: Forest development costs are capitalised to cost of forest, and all other costs are written off (Opio, 1999).

#### **Evergreen Forests Ltd.**

Development Forests: All costs incurred in acquiring, establishing cultivating and financing are recognised as a forest asset;

Production Forests are managed on a sustainable yields basis (so that) all costs of harvesting and re-establishing or cultivation of subsequent rotations are recognised as an expense in the current year;

Financing: Interest is capitalised to Development Forests based on the avoidable funding costs to the Group of the development forest crop;

Carrying Value: Directors obtain an independent valuation based on the net present value of the collective forest crop (Evergreen, 2002).

### **3.6 Pre-SGARA Accounting Practice in Australia**

In Australia the situation was no different. In addition to detailed analysis of company accounts there were three principal studies into prevailing accounting practice for agricultural entities. The first is a general overview across a significant sample of SGARA-listed entities whilst the other two relate to surveys and analyses by Herbohn *et al.* (1998) of reported accounting practices and policies in listed- and private-forestry entities and for the State Government Forestry agencies.

#### **3.6.1 Analysis of Top-500 ASX-Listed SGARA Companies**

Dowling and Godfrey (2001) recorded a broad overview of accounting policies adopted by agricultural entities in the Top-500 ASX-listed companies prior to formal adoption of the new SGARA AASB 1037 standard. Their study was based upon the 1999 annual reports for 31 companies. One objective was to determine whether the requested deferral in implementing the new standard was warranted because of the stated need for significant changes to internal measurement, reporting and accounting systems. They concluded the claim was valid since only a few entities were using the proposed ‘market value’ approach contained in AASB 1037.

The list of Australasian agricultural reporting entities is recorded in [Appendix 3](#) with companies shown in **bold** that were identified in the ASX-industrial classification by Dowling and Godfrey (2001, Table 1). Since the ASX broad classification system was not helpful for identifying SGARA-type, Dowling and Godfrey recast and summarised the SGARA-types represented amongst the 31 listed reporting entities.

***Table 6. SGARA Types within ASX Top-500 Entities in 1999***

<b>SGARA Types</b>	<b>Number of Firms</b>	<b>%</b>
Crops	3	10
Grapevines	12	40
Livestock	8	27
Standing Timber	11	37

Source: Dowling and Godfrey (2001), Table 2.



Two companies reported three types of SGARAs – these were unidentified, but might have comprised Tandou Ltd., which carried cereal crops/cotton and grapevine assets, and Newhaven Park Stud Ltd., which carried two separate types of livestock assets, *i.e.* non-thoroughbred horse trading inventories and stud mare/stallion interests.

Dowling and Godfrey described the diversity of measurement methods disclosed, including 14 companies using more than one valuation method. One entity declined to disclose its measurement method.

***Table 7. Disclosed SGARA Measurement Methods in ASX Top-500 Entities***

<b>SGARA Valuation method</b>	<b>Number of Firms</b>	<b>%</b>
Historical cost (HC)	18	60.0
Net present value (NPV)	4	13.3
Net market value (NMV)	4	13.3
Independent/directors' valuation	11	36.7
Lower of HC or net realisable value	6	20.0

Source: Dowling and Godfrey (2001), Table 3.

Table 7 indicates that, in the 1999 reference period, the least-used valuation methods were NMV, which was the required reporting basis under AASB 1037, and NPV, which was a permitted surrogate if NMV could not be determined. Thus many firms would require changes to their accounting reporting policies even if internal management practice remained unchanged. *'The limited use of NMV implied that active and liquid markets do not exist for some SGARAs, or that firms preferred not to measure SGARAs at NMV'* (*ibid.*, p. 48). It was evident that for three early-adopter entities multiple valuations pertained. One forestry company used HC for the forest asset and NMV to measure timber. For the other two, one used a combination of HC, for its juvenile trees, crops and livestock, and then NPV as a surrogate for NMV thereafter; whilst the other company used NPV and independent valuations to measure grape-vines.

Dowling and Godfrey noted an early-indicated consequence of multiple valuation methods was that a stated objective underpinning the new AASB 1037 standard would not be achieved; that is, to obtain consistent inter-company valuations related to external market values.

Dowling and Godfrey further analysed the two previous Tables to determine whether particular measurement methods were preferred or deemed more relevant for particular SGARA-types. The 30 companies used a total of 51 measurement methods because of multiple valuation methods adopted under their pre-SGARA accounting policies in the absence of an approved accounting standard.

**Table 8. Disclosed Measurement Methods by SGARA Types**

SGARA Types	Historic Cost - HC	NPV	NMV	=<HC or NRV	Ind/Dir Valns.
Timber [n=11]	7 63.6%	2 18.1%	2 18.1%	2 18.1%	2 18.1%
Grapevines [n=12]	9 75.0%	1 8.3%	2 16.7%	0 -	8 66.7%
Livestock [n=8]	3 37.5%	0 -	2 25.0%	4 50.0%	1 12.5%
Crops [n=3]	3 100.0%	1 33.3%	2 66.7%	0 -	0 -

Source: Dowling and Godfrey (2001), Table 4.

These findings are broadly equivalent to the various pre-IFRS valuation guidelines recommended in New Zealand. Typically, horticultural assets were maintained at historic cost until ‘commercial’ maturity, usually three to four years after planting. The assets were then either revalued, representing modified-historic cost; or, an independent valuer provided market valuations for the established orchard/vineyard and associated long-life improvements to land. Rarely were the SGARAs themselves disaggregated from the integrated horticultural orchard or vineyard assets.

Livestock valuation methods appear to indicate reporting entities might be operating with two separate classifications. Bloodstock ‘fixed’ assets were carried at modified-historic cost adopting directors’ valuations, and ‘trading’ livestock as inventory at the lower of historic cost and net realisable value, reflecting current accounting practice.

Short term crops were typically valued at net market value. However each of the three reporting entities also valued crops at historic cost. The reason was not given. Possibly ‘cost’ reflected use of forward sale contracts, *e.g.* for cotton or sows. In the pre-IFRS era this would differ from NMV at harvest, as prescribed by the SGARA standard.

Dowling and Godfrey concluded by predicting that SGARA-entities would face major changes to their financial reporting policies and practice on adoption of NMV under

AASB 1037 (2001, p. 50). This justified deferred implementation of the new standard but with a resultant likelihood of continuing controversy over the treatment of measurement gains and losses and consequent greater volatility in earnings. Their predictions proved to be correct.

### **3.6.2 Pre-AASB 1037 Forestry Valuation and Accounting Practice**

Although prepared in 1997/98, the original Herbohn and Herbohn (1999) feature article on *Accounting for Forests in Social, Economic and Political Contexts* discussed implications of the proposed AASB 1037 SGARA standard.

The article reported a postal survey of forest managers. Reasons were discussed for removal of mandated non-financial environmental disclosures from the original DP 23 proposal (Roberts, Staunton and Hagan, 1995). Survey participants were opposed to mandated regulation. They appeared to dislike introduction of volatility in 'bottom-line' reporting from current value market valuations and recognition of changes in values of forest assets.

The conclusion was that an in-depth examination of existing practice was required from a larger survey sample across the private and public sectors. This occurred in the second article (Herbohn, Peterson and Herbohn, 1998). Both articles indicate lack of common forestry accounting policies and wide disparity in forestry valuation techniques and reporting practice prior to the AASB 1037 standard.

The Herbohn *et al.* survey was conducted in the context of the release the SGARA Discussion Paper No. 23 (Roberts *et al.*, 1995) and Exposure Draft ED 83 (AARF, 1997). They repeated the forestry accountants' accounting 'problem' (pp. 54-5):

biological growth and a long productive cycle make these assets difficult to deal with conceptually and practically. Biological growth results in increases in both timber volume and quality which creates problems for asset measurement and revenue recognition [with] elapse of long periods between establishment costs and generating revenue through harvest. Major questions include whether value changes associated with growth and market conditions should be recognised as they occur or when they are realised. If [the former] should they be treated as capital or income adjustments, or some combination of the two?

Herbohn *et al.* (1998) found actual practice varied considerably. This was attributed to existing GPFR-standards specifically excluding agricultural regenerative activities. As in New Zealand, reporting entities therefore devised their own policies.

The sample included seven ASX-listed forestry companies and an additional private-sector company, North Limited, and five state-forestry authorities. Each provided financial statements for the 1990-95 periods. All eight private-sector entities responded but only six of the seven State authorities co-operated. The Northern Territory Authority was excluded because it did not disclose any significant forestry investments (*ibid.*, p. 59).

These results pre-date the Dowling and Godfrey (2001) analysis but complement it by identifying more comprehensively the variety of existing practice adopted by individual forestry reporting entities listed in the ASX Top-500 shown in Table 8.

Herbohn *et al.* sought to determine current forestry accounting practice for:

- valuation methods for forestry assets;
- recognition and measurement of value changes;
- balance sheet classification of forestry assets; and
- disclosure of non-financial environmental information.

The variety of valuation methods, timing and bases for recognition of value changes, and balance sheet treatment for individual companies is contained in Tables 3-5 in Herbohn *et al.* (*ibid.*, 1988, pp. 59-63). These are reproduced in full in [Appendix 4](#).

Three of the State Forestry Authorities prepared their financial statements only on a cash basis. These were not suitable for analysis against each of the first three practice criteria. They were the Department of Conservation and Land Management (WA), the Department of Conservation & Natural Resources (Vic.) and Queensland Department of Primary Industries (QDPI).

In summary the Herbohn *et al.* survey results showed:

- most State Authorities prepared only cash-based financial statements, recording forestry assets without valuations, with only slow progress to accrual accounting;
- private-sector entities were evenly divided between those adopting historic cost variants and those providing some alternative form of current valuation. The latter used NPV as a valuation surrogate for recoverable amount. Typically there was no supplementary current market value information in Note disclosures;
- this indicated lack of any active secondary markets to value forestry assets;
- disclosures tended to be minimal especially for discount rates and assumptions used. Any valuation change was booked as a capital maintenance adjustment to reserves, which would reverse to income when the forest was harvested or sold; and
- none of the recognition measures fully conformed to proposals in DP 23 or, subsequently, in the AASB 1037 *SGARA* standard (*ibid.*, p. 61).

The final Herbohn *et al.* conclusion was that ‘*until the issue of measurement...and how asset value changes should be reported*’ and a theoretical reporting framework were developed for SGARAs, it was premature to be devising an accounting standard for them (*ibid.*, p. 65).

### **3.7 Summary of Australasian pre-SGARA Accounting Practice**

General purpose financial reporting practice for primary producers evolved for:

- use of net current values at harvest for ‘consumable’ agricultural products where established markets existed; but where that was inappropriate, then lower of market value or cost was typically used, *e.g.* by ‘bearer’ entities with integrated operations;
- unrealised holding gains for changes in volume or numbers, *e.g.* for trading livestock, were reported as a component of operating profit, but where market price fluctuations could be determined these were credited to equity reserves for capital maintenance;
- stud animals were recorded at net current value, or at modified-historic cost with revaluations recorded in equity as part of separate revaluation reserves, sometimes partially off-set by a deferred taxation reserve. Assets held at modified-historic cost were depreciated by adopting useful-life bases as for other non-agricultural assets;

- perennial horticultural assets were treated for accounting purposes as integrated assets with the land and infrastructure improvements supporting that horticultural activity. Sometimes horticultural land was dis-aggregated from integrated horticultural assets. For these ‘bearer’ entities, accounting measurement and valuation practice tended to adopt equivalent policies to others of their non-agricultural activities and assets;
- forestry activities and forest asset valuations had no settled accounting guidelines, practice or procedures. Treatment of forest valuations varied between reporting entities.

### **3.8 Role of the Profession prior to Issue of the New Agriculture Standards**

The Profession’s objective in Australia and New Zealand was to identify and establish accepted authoritative support for accounting rules and guidelines for agricultural sectors. The aim was to identify first-principles, best-practice bases for recording and reporting consistent accounting policies. In the process, distinctions were drawn between types of agriculture relating to ‘consumable’ and ‘bearer’ activities.

The issue was most visible for the major Australasian publicly listed agricultural companies. In Australia, these included major primary sector forestry, wine, arable and livestock companies such as Amcor Ltd., Australian Agriculture Company Ltd., BRL Hardy Ltd., CSR Ltd., Foster’s Ltd., Gunns Ltd., Select Harvests Ltd., Southcorp Ltd. and Tandou Ltd.

Each of these major companies reported biological activity in disparate ways in their audited financial statements through use of recommended professional guidelines in combination with other existing accounting standards; or, they devised their own policies.

In New Zealand, the three major forestry companies, NZ Forest Products Ltd., Fletcher Challenge Ltd. and Carter Holt Harvey Ltd. were amongst the largest and longest-established listed companies; the latter two were also listed on the ASX. Each had widespread local and international corner-stone shareholdings held by major American or Australian investors thereby increasing diversity in reporting practice.

Inconsistent forestry financial reporting policies encouraged the NZSA to try to obtain consistent practice and reporting. Their efforts failed. There was no conformed basis agreed by the profession and auditors, or for benefit of investors and other users. This lack of success could be attributed to the NZSA having insufficient countervailing power relative to the major forestry companies to agree upon, let alone impose, a common accounting and reporting standard for the forestry sector.

### **3.9 Summary**

This diversity of practice across Australia and New Zealand, particularly in forestry valuation methods, and the variety of agricultural sector accounting practice, created the practical accounting issue of inconsistent annual company reporting and the lack of individual inter-entity comparability. There was a general reporting issue to resolve. Another reason was the general exclusion of Agriculture from existing GPFR standards.

By 1990 conditions were ready for agenda access to consider appropriate accounting principles for agricultural activities. However, there was no external crisis *'event, or triggering mechanism, [to] transform the problem into an issue...[as] an agenda item'* (Cobb and Elder, 1983, p. 85).

Instead, respective Australian and International standards setters were encouraged to initiate their internal consideration processes for other unrelated reasons.

## Section 4. RULE-MAKING PROCESSES FOR THE NEW SGARA AND AGRICULTURE STANDARDS

### Introduction

Development of new accounting standards for Agriculture derived from two distinct sources. The first was promoted in Australia from 1988 and the other by the IASC in 1993. Each standard had themes in common, but evolved differently until they later converged as the IAS 41 standard. This section traces the evolution of the new *SGARA/Agriculture* standards through each of their agenda-entrance and rule-making consideration stages.

***Table 9. Agenda Rule-Making Processes Summary***

Rule Making Stages	Elements	Modes of Lobbying	Evidence
<b>Agenda Entrance</b>	1. Issue emerges and gains admission to agenda	Discussions with members of regulatory bodies, politicians, <i>etc.</i> ; pressure through media reports, campaigns	Surveys, government reports; newspaper and other media comment
<b>Formal Consideration of Agenda Items</b>	2. Discussion memorandum or paper drafted and released	Written submissions, informal discussion	Written submissions
	3. Exposure draft(s) prepared and released	Written submissions, informal discussions	Written submissions media releases
	4. Standard prepared, approved and issued	Press releases; meetings of professional bodies; contact with regulators and politicians	Text of standards/policy notes

Source: Simplified Table 1 from p. 12, Section 2.

The Elements in Table 9 comprise the four chapters in this section:

- chapter 1 examines the issue access, agenda creation and entrance stages accepted respectively by the AARF/AASB in Australia and the IASC Board in London;
- chapter 2 studies the *SGARA* Discussion Paper No. 23 (DP 23) in Australia and the IASC Agriculture SC's *Draft Statement of Principles* (DSOP);
- chapter 3 discusses the bases for the respective *Exposure Drafts* developed by the gatekeepers. Each differed materially from criteria in chapter 2; and
- chapter 4 considers the gatekeepers' role and the political processes prior to issuing each of the AASB 1037 *SGARA* standard and the IAS 41 *Agriculture* standard.



## Chapter 1. AGENDA ENTRANCE FOR THE NEW AGRICULTURE ACCOUNTING STANDARDS

### Introduction

The issue creation and agenda entrance rule-making stages were generated internally in Australia and facilitated externally for the IASC to establish new agriculture topics onto respective Board agendas. These occurred independently from November 1988 to about end-1993 in Australia; and from 1989 intermittently until the IASC Board agreed the *Agriculture* proposal be accepted formally onto its agenda in March 1996.

***Table 10. Agenda Entrance Rule Making Process for Agriculture***

Stage of Rule Making	Elements	Modes of Lobbying	Evidence
<b>Agenda Entrance</b>	Issue emerges and gains admission to agenda sponsored by members within the regulatory bodies.	No external lobbying.	AARF <i>Project Brief</i> IASC <i>Point Outline</i>  Source material not published before

Source: Table 9 modified for the *SGARA/Agriculture* standards processes.

The proposals were developed virtually without external discussion or encouragement, other than by the World Bank in the case of the IASC. The common link for each initiative was that respective standard-setter agencies, for their own reasons, sought to bring accounting and reporting for agriculture within the evolving general purpose financial reporting (GPFR) conceptual framework.

This chapter discusses the role of the influential ‘key player’ initiators, and the political processes adopted for the initial issue creation and agenda entrance stages. Each represented examples of the Cobb *et al.* (1976) *inside access* model. In Australia, the principal promoters were Robert Keys, with AARF staff, and Warren McGregor as AARF Executive Chairman. McGregor was also an IASC Board technical adviser. In London, the IASC Secretary-General, David Cairns, introduced an external World Bank initiative to his Board which then established work programmes for staff and its Agriculture SC, under Project Manager Ian Kirton, also reporting to the IASC Board.

## **1.1 Issue Creation and Agenda Entrance in Australia**

In 1988/89 the Australian Accounting Research Foundation (AARF), on behalf of the Accounting Standards Review Board (ASRB) and the Public Sector Accounting Standards Board (PSASB),<sup>24</sup> established a number of research projects including a Proposed Statement of Accounting Concepts within a Conceptual Framework, the *Objective of General Purpose Financial Reporting* (AARF, 1990b), *Definition and Recognition of Revenue* (AARF, 1990c), and *Definition and Recognition of the Elements of Financial Statements* (AARF, 1992). As a result of these activities the AARF decided internally to bring agriculture into mainstream reporting standards because relevant existing accounting standards had specifically excluded accounting for agricultural activities.

### **1.1.1 AARF Contracts UNE to Help Develop the SGARA Project**<sup>25</sup>

On 10 May 1989, Don (D.L.) Roberts, Practitioner in Residence at the University of New England (UNE) wrote to the AARF requesting advice on whether *'the Accounting Profession had issued accounting standards for accounting for forestry and livestock'*.

On 23 May 1989, Ms B.T. Curran, AARF Technical Director - Accounting, replied that *'the subject of self-generating and regenerating assets'* had been added to the work programme of the AARF and PSASB.<sup>26</sup> *'This project will involve the preparation of a discussion paper for input into development of a Statement of Accounting Standards on that subject. In [its] absence no particular methods of accounting for livestock or forests would at present be precluded by the accounting profession'*.

This was already an internal initiative confirmed by the above external enquiry. In addition to evolving conceptual criteria, the standards 'gap' in accounting for agriculture provided an underlying trigger to create the topic and enter it onto the formal AARF agenda. Another internal reason for initiating agenda entrance was confirmed much later.

<sup>24</sup> Appendix 5 provides an overview of the early relationships between the AARF, AASB and PSASB.

<sup>25</sup> The writer is indebted to Dr J.J. Staunton for access to his private work-papers covering this project.

<sup>26</sup> This is the first independently quoted reference found for 'self-generating and regenerating assets' (SGARAs) – reputedly attributed to Robert Keys within the AARF.

The purpose of the proposed discussion paper was to *'form a basic educative tool in ensuring Board Members and staff alike are well informed of accounting issues involved [on this topic] and well-versed in valuation alternatives to this field of interest'*.

The letter described the role of a proposed Project Advisory Panel. This would comprise up to six members with an independent contractor, yet to be appointed, reporting to it; and, given his interest, Roberts was invited to apply or to provide project oversight. The panel would assist the contractor by *'acting as a sounding board against which ideas can be bounced to ensure the paper is comprehensive and thoroughly researched'*.

Don Roberts accepted in principle. On 23 August 1989, the AARF formally proposed that he be appointed as the project contractor, for a modest \$6,000 fee. The offer included both a draft contract for Preparation of a Discussion Paper, entitled *Accounting for Self-Generating and Regenerating Assets* and a prescriptive draft *Project Brief*.

Over the course of the next year, and in order to broaden the opportunity for different departmental teams to consider wider scope matters in the *Project Brief*, the contract was amended so that the Department of Accounting and Financial Management at UNE, under Professor G.G. Meredith, became the contractor with D.L. Roberts as *Project Leader – Self-Generating Assets Research*.

Eventually, agreement was reached on 13 July 1990 between the AARF, signed by Warren McGregor as Director, and the UNE for an increased \$10,000 fee together with a revised *Project Brief*.<sup>27</sup> This is a significant unpublished historical record since its content, identification of issues and contractual prescriptions were instrumental in determining the evolution of the eventual standard. It is included in full as [Appendix 6](#).

The Brief provided insight into internal AARF thinking at the time. The principal aim was to align the contracted work, and recommendations, with the AARF's evolving Conceptual Framework and Proposed Statements of Accounting Concepts for GPFR.

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<sup>27</sup> N.B. The Department estimated it would cost at least \$100,000 *p.a.* to service the project; Staunton Papers.

Initial UNE tasks were to define what was meant by SGARAs; their appropriate measurement basis; timing of revenue recognition and disclosure issues, with worked examples to assist analysis of recommendations and to determine how choices were made amongst alternatives.

In his cover letter, Warren McGregor expressed concern that the project was expected to take 21 months before a first draft would be ready for review '*given the pressing need for guidance in this [SGARA] area*'. The pressing need was not disclosed.

Regardless, the Parties agreed the Report should be completed by June 1992 with a final draft to be provided by end-March 1992. The first UNE quarterly report was contracted for end-March 1991. This was supplied on 15 January 1991.

The UNE initiated a number of work streams internally to meet the timetable for first draft by December 1991 and final draft by March 1992. This proved too ambitious.<sup>28</sup>

In December 1991, an undergraduate honours student, Ms M. Goyen, with Roberts, produced Project Working Paper, 91-3. In keeping with the GPFR criterion, the paper identified the potential user groups as recipients of financial statements for agricultural entities; namely, Resource Providers, Recipients of Goods and Services, Parties Performing Oversight and Review Functions, the Commissioner of Taxation, and Management. The *Project Brief* had excluded 'Management' from consideration being a special-purpose user.

Working Paper, 91-3 identified an initial definition for 'agriculture' within the conceptual framework concepts. The UNE group proposed:

self-generating and regenerating assets are non-human living assets which, due to inherent capacity for growth, production, procreation and de-generation, contain economic benefits and service potential which are subject to continual variations during their lifetime (Goyen and Roberts, 1991, p. 9).

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<sup>28</sup> The final report was published in May 1995.

A simple 'plant' and 'animal' classification scheme was proposed with physical sub-tiers by biological type split between short- and long-term SGARA component sectors, and between current- and non-current assets in financial attribute terms.

The significance of the original Don Roberts query to the AARF in May 1989 became apparent:

the relative economic importance of some particular Australian SGARA deserves individual consideration. The two SGARA of interest to any research project because of their significant economic importance, unique characteristics and some controversy as to appropriate accounting treatment, are the Australian forestry and livestock industries (*ibid.*, p. 2).<sup>29</sup>

Goyen and Roberts identified relevant principles for potential biological, economic and financial classification schemes as required by the *Project Brief*. 14 major agricultural biological sector classes were identified in Australia alone, with more than 100 specified agricultural products. This encyclopaedic description of agricultural activities and products and their life-cycles made a simple classification system problematic. Indeed, a forlorn hope where '*possession of life*' was a key characteristic and therefore classifications '*responsible for the growth, change and loss through mortality*' had profound implications for financial representations of SGARAs for accounting purposes (*ibid.*, p. 15).

The initial taxonomy classifications were summarised as: Self-generators, Regenerators, or both; Length of lead time; Length of economic life; Number of outputs; Nature of output; Nature of production cycle; Level of control over production process and Quantifiability of Inventory.

After discussing various characteristics and classifications, Goyen and Roberts concluded:

the main economic attribute to be accounted for with respect to SGARA is the life of the plant or animal. This life is responsible for the economic flows that are of a value to the producer. Market based values reflect these economic attributes in financial terms. Presentation in the financial statements would be improved, in many cases, by the inclusion of a third intermediate asset classification [in the balance sheet], supported by the additional disclosure of physical data (*ibid.*, p. 35).

The following year, in September 1992, the Department published Working Paper, 92-3.

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<sup>29</sup> These two sectors, forestry and livestock, were to dominate the agriculture standard design in Australia.

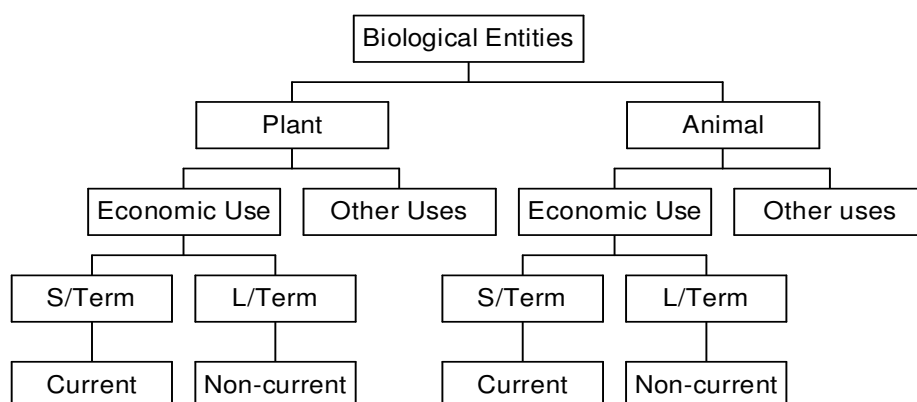
An objective was to align with the agreed framework of broad accounting concepts (ASRB, 1990).

The principal elements in Working Paper, 92-3 were:

- the SGARA definition remained unchanged from Working Paper 91-3 and was confirmed as ‘consistent with the definition of assets generally found in Statement of Concepts SAC 4’ (AARF, 1992); however
- the classification taxonomy had evolved significantly: ‘in view of severability, mobility and reproductive mechanisms a productive classification may be between animal life and plant life’ (Staunton, J., D. Roberts and L. Hagan, 1992, p. 1).

WP 92-3 provided the first SGARA classification taxonomy:

Figure 1. SGARA - A Simple Classification Approach



Source: Staunton *et al.* (1992), Table 1.

Staunton *et al.* distinguished between ‘those SGARA whose product is final and consumable, thus terminating the service potential of the SGARA in the reporting entity...[so that] economic value must terminate when there is no residual value left as a SGARA’, *i.e.* on harvest or death. These SGARA were defined as ‘consumables’.

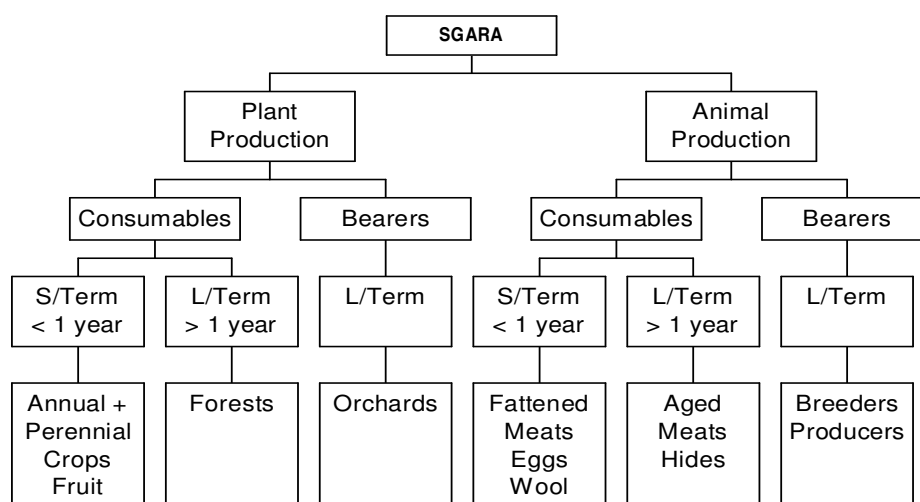
However,

some SGARA may produce consumables on an ongoing basis without terminating and thus retain their service potential and have residual value. In economic terms, these were stated akin to durables but this would be a misnomer for assets, which in the next period can revert to a consumable. Better for these purposes might be the classification “bearers”, which connotes a productive process leading to separable products (*e.g.* eggs, offspring, fruit, wool) (p. 3).<sup>30</sup>

<sup>30</sup> This was the first discussion about ‘consumables’ and ‘bearers’ as required by the *Project Brief*. This is developed further in the DP 23 discussion in the next chapter.

Accordingly, WP-92-3 recommended a revised taxonomy to reflect better the key ‘*plant and animal dichotomies*’ and the GPFR financial reporting category linkages for SGARA classifications split between short-term inventories and long-term assets.

Figure 2. Extended Economic Taxonomy for SGARA Classifications



Source: Staunton *et al* (1992), Table 2.

The authors’ focus was on *plant* - with forests as the proxy for that class, and *animal* - with trading livestock as its proxy. The aim was to develop accounting for these two sectors. UNE preoccupation was to determine accounting, valuation and reporting processes for the more complex forestry sector with its different types of forest resources.<sup>31</sup> This was designed to meet SAC 1 *Reporting Entity* (AARF, 1990a) criteria for both the corporate sector and the various types of government trading enterprises (Staunton, 1993).

*‘This taxonomy has the advantage of being relatively simple and extendible into the required financial concepts of “current”, “non-current”, “inventory” and “machinery” found in the various statements of accounting concepts’* (Staunton *et al.*, 1992, p. 3).

Staunton *et al.* also discussed the lack of consensus and a clear theory for SGARAs. Since these were excluded from existing standards, it was necessary to fill the ‘*theoretical voids*’ for the range of SGARAs relative to the conceptual framework.

<sup>31</sup> Identified as native forests, forestry concessions and hardwood and softwood forestry plantations.

They identified 'key topics' and related 'issues for further research'. Each was ranked in order of conceptual importance for departmental work-streams and inclusion in the eventual Discussion Document. Reference criteria were derived from a *Tentative Building Blocks of a Conceptual Framework for General Purpose Financial Reporting* diagram (AARF, 1990b). Forty-two issues were identified. These were distilled into four major topics and fifteen sub-topics with cross-references to AARF's 1990 conceptual framework.

The purpose of WP 93-2 was therefore to set '*the scene...for further research on the identified issues...(including) review of literature relevant to SGARA, or examination of regulation concerning SGARA and a review of the reporting practices of reporting entities concerning SGARA*' (Staunton *et al.*, p. 3).

With this ambitious and extended agenda it took a further 2½ years for these matters to be resolved sufficiently for publication as Discussion Paper, No. 23 (DP 23) (Roberts, D., J. Staunton and L. Hagan, 1995) as required under the original AARF contract. Given Warren McGregor's earlier misgivings about the extended time expected, the AARF had also initiated its own internal project. Subsequently this superceded the UNE work.

### **1.1.2 Summary**

Don Roberts and the UNE were independent external contractors rather than insider gatekeepers. Their relationship was arms-length. There was no decision-making responsibility, nor recorded participative role with the AARF sponsors.

Thus, issue access and creation had occurred internal to the AARF. The AARF's prescriptive *Project Brief* in [Appendix 6](#) was significant. Cobb and Elder noted '*how the problem is defined has the effect of structuring subsequent choices by circumscribing its solution possibilities*' (1983, p. 175). The history of the agriculture standard was influenced *ab initio* by the nature of the defined biological characteristics in the *Project Brief*. This limited definition restricted consideration of alternatives.



## 1.2 IASC Issue Creation and Agenda Entrance

The impetus for creating an international accounting standard for agriculture was from an entirely different source to that in Australia.

In 1989, the IASC initiated work to determine the *Financial Reporting Needs of Developing and Newly Industrialised Countries* (IASC, 1990). This was then placed on hold for two years in favour of the higher priority IASC *Improvements Project* until resurrected in the IASC's 1992 future work programme:

agriculture is important to the economies of many countries, both developing and developed, and gives rise to a number of difficult accounting issues related to crops, plantations and livestock (IASC, 1992, July).<sup>32</sup>

At the time, in the early 1990s, the IASC Board met three times a year with responsibility for approving exposure drafts and new international accounting standards. It comprised representatives of the professional accountancy bodies in 13 countries and up to four other organisations with an interest in financial reporting. There was also a Consultative Group which commented on all aspects of the IASC work programme. This Group included representatives of international users groups; development agencies, the World Bank and International Finance Corporation; the FASB and the EC. Representatives were able to participate in IASC Steering Committees. The IASC also worked with the national standard-setting bodies and with Securities Regulators such as IOSCO (IASC, 1993, July).

Camfferman and Zeff (2007) noted '*the trend towards appointing delegates having standard-setting experience or a technical background...Warren McGregor (was) technical-director accounting at the Australian Accounting Research Foundation (and) became the first regularly attending staff observer in 1986*' (p. 70).<sup>33</sup> '*Staff observers were at that time providing technical support for national standard setters*' (p. 220). However, '*even though they were known as observers, several distinguished themselves over long periods by the contributions they made at board meetings and their service on key steering committees, including...Warren McGregor from 1986-99*' (p. 225), i.e. during development of the IASC's *Agriculture* standard from the mid-1990s.

<sup>32</sup> N.B. In this context 'plantations' referred, for example, to rubber, palm oil or tea plantations; not forestry.

<sup>33</sup> W. McGregor was also signatory to the contract with UNE in July 1990; refer [Appendix 6](#).

Originally the proposal for an agriculture standard was conceived by the IASC to help developing countries. The initiative was promoted by the World Bank since agricultural development projects accounted for approximately 20% of the Bank's total lending. The World Bank and other development agencies sought adoption of consistent financial treatment and reporting for like-transactions by their developing- and newly-industrialised country clients. This would assist accountability for funded development programmes, especially for timber concession and other primary sector projects (IASC, 1992).

In 1992, the IASC reinstated work on *Financial Reporting Needs of Developing and Newly Industrialised Countries* after a meeting of the United Nations Intergovernmental Working Group on International Standards of Accounting and Reporting. This followed discussion by the IASC Secretary-General, David Cairns, with regional accountancy bodies including the Council of the Eastern, Central and Southern African Federation of Accountants (ECSAFA) in Cape Town in May 1992.

It became apparent to Cairns from those discussions with ECSAFA and others about reporting needs for financial reporting in developing countries that there would be great support for IASC projects on agriculture and extractive industries for consideration by both the Board and a project Steering Committee (IASC, 1992, July; Camfferman and Zeff, 2007, p. 290). Staff were asked to consider project proposals and to develop recommendations for consideration by and Board approval during 1993.

The IASC noted wider interest in the topic. The ASEAN Federation of Accountants 'has established a joint Accounting Standards Committee...to develop accounting standards needed by such industries as plantations, forestry, mineral extraction, shipping, dairy farming, hotel and tourism, property development and aquaculture' (IASC, 1993). In June 1993, the Board decided to discontinue its *Financial Reporting Needs of Developing and Newly Industrialised Countries* study and instead focus upon specific issues of particular importance to them, such as issues relating to agricultural livestock, growing crops and plantations noting '*the staff intends to develop project proposals on agriculture issues for consideration by the Board in 1994*' (IASC, 1993, July).

This shift in emphasis was facilitated by Randolph Andersen at the World Bank. He proposed to Cairns that it was *'interested in improving accountability and transparency by its developing-country borrowers, and that the Bank would probably be willing to fund a relevant IASC project'* (Camfferman and Zeff, 2007, p. 402). The discussion focussed on a standard on agriculture. The project gained impetus and Board support when in 1994 the World Bank agreed to a US\$ 531,000 grant [approximately £350,000] (IASC, 1996c).

The IASC's Annual Review (IASC, 1994) noted agreement to add the project to its formal work programme; but *'the Board's approval was not given enthusiastically, and then mainly because of the World Bank grant'* (Camfferman and Zeff, 2007, p. 402).<sup>34</sup>

The Board approved the Agriculture project at its June 1994 meeting, including appointment of an Agriculture Steering Committee (SC). The SC's brief was to report back with a *Point Outline* to the Board at its March 1996 meeting. The summary rationale for the project was:

while Agricultural enterprises can and do apply the same accounting standards as other enterprises, agriculture gives rise to a number of accounting issues which are different from those that arise in other industries. As agriculture is a significant industry in many countries, particularly developing countries, the Board added a project to its work programme which will deal with the recognition, measurement and disclosure of assets, liabilities, income and expenses resulting from growing crops, plantations and forestry, and livestock.

The project will draw on existing IAS, the IASC Framework and the work of the national standard setting bodies. The project will include consultation with financial institutions, including development banks, that are providing finance and assistance to agricultural enterprises as well as agricultural enterprises themselves. The IASC also intends to appoint consultants from a number of developing countries to assist with the research (IASC, 1994).

The project proposal was a confidential board memorandum at the time and has not been reported before.<sup>35</sup> It is attached as Appendix 7A and serves several purposes: as

- an historical reference to and comparison with the earlier *AARF Project Brief*;

<sup>34</sup> Several delegations questioned whether the IASC should take up Agriculture. In November 1994, Cairns wrote to Eiichi Shirator, IASC Chairman *'Are we sure we want to do this project? I have not heard a good word about it - apart from the South Africans'*, Camffermann and Zeff (2007, p. 402, & end-note 311).

*N.B.* Cairns probably meant 'the Australians'.

<sup>35</sup> It was obtained on application to the IASB who also provided the confidential *Project Outline*, accompanying Board Paper, and an associated Staff Note Agenda Item commenting on developments subsequent to the *Point Outline* and preparatory to presenting the *Draft Statement of Principles*.

- reinforcement of the formal rule-making stages whereby the IASC's internal objectives, expectations and reporting processes were clearly identified in the project proposal through all work programme stages;
- confirmation there was a recognised need internally for a new standard because of omissions from other approved standards and the identified unique features for agriculture in a country, regional and international context; but acceptance that
- the proposed full work programme was recognised as reasonably optimistic for target completion in 1998 and not without risk due to dealing with unfamiliar issues and new recognition and disclosure issues with consequent potential for delay.

### 1.2.1 IASC's Standard Setting Practice

In 1990, the IASC established a comprehensive model for its standard-setting deliberation processes, similar to those adopted by the FASB.

The agenda initiation and consideration stages, and the roles and responsibilities of the IASC's constituent insiders required to develop a new topic for eventual consideration by the Board was prescribed as follows:

'Board representatives, Member Bodies, members of the Consultative Group, other organisations and individuals and the IASC staff are encouraged to submit suggestions for new topics which might be dealt with in International Accounting Standards. From time to time, the staff prepares project proposals which set out reasons why particular projects should be added to the current work program

'Once the Board has added a topic to its work programme, it sets up a Steering Committee to develop a Statement of Principles, an Exposure Draft and, ultimately, an IAS. Each Steering Committee is chaired by a Board Representative and usually includes representatives of the accountancy bodies in at least three countries. Steering Committees may also include representatives of other organisations that are represented on the Board or Consultative Group or which are expert in the particular topic.

'The development of every IAS includes:

- identification and review of all the accounting issues associated with the topic;
- consideration of the application of the IASC's Framework for the Preparation and Presentation of Financial Statements to those issues;
- study of national and regional accounting requirements and practice, and other relevant material on the topic;
- detailed review by the Steering Committee of the issues, national and regional accounting requirements and practice, and other relevant material;
- detailed review by the Board of the Steering Committee's recommendations;
- consultation with the Consultative Group, Member Bodies, standard setting bodies and other interested groups and individuals on a world-wide basis;

- public exposure of the draft IAS;
- evaluation by the Steering Committee and the Board of the comments received on the Exposure Drafts' (IASC, 1992, July).

'The role of a Steering Committee was defined the following year.

Each Steering Committee:

- reviews the issues associated with the topic along with national and regional accounting requirements and practices, existing and proposed IASC pronouncements, and other relevant material;
- advises staff on the issues to be addressed and areas for research;
- evaluates comments on the Draft Statement of Principles and Exposure Draft; and
- carries out the instructions of the Board on the approach to be taken on particular issues' (IASC, 1993).

'The internal procedure for developing an International Accounting Standard (IAS) was further elaborated:

- the Steering Committee considers the issues involved and develops a Point Outline;
- after receiving comments from the Board on the Point Outline, the Steering Committee prepares a Statement of Principles. The purpose of this Statement is to set out the underlying accounting principles that will form the basis for the preparation of the Exposure Draft. It also describes the alternative solutions considered and the reasons for recommending their acceptance or rejection;
- the draft Statement of Principles is circulated to Member Bodies, members of the Consultative Group and other organisations for comment;
- the Steering Committee reviews the comments on the draft Statement of Principles and agrees a final Statement which is submitted to the Board for approval;
- the Steering Committee prepares a draft Exposure Draft based on the Statement of Principles approved by the Board. The draft Exposure Draft is submitted to the Board for approval. After revision and with the approval of at least two-thirds of the Board, the Exposure Draft is published. Comments are invited from all interested parties during the exposure period, usually six months;
- the Steering Committee reviews the comments and prepares a draft International Accounting Standard; and
- the Board reviews the draft IAS. After revision and with the approval of at least three-quarters of the Board, the Standard is published. [*N.B. Emphasis added.*]

'During this process, the Board may decide that the needs of the subject under consideration warrant additional consultation or would be better served by issuing a Discussion Paper for comment. It may also be necessary to issue more than one Exposure Draft before the Board approves an International Accounting Standard.' (IASC, 1993, July).

These IASC institutional processes are primarily inwards-focussed. They correspond to the *inside access* agenda process (Cobb *et al.*, 1976), but with any external *mobilisation* only occurring late in proceedings. One consequence is that lobbying becomes less likely to be successful on points of principle. Too much institutional time, reputation and capital would have been invested to concede material revision or delay to the agenda timetable.

During the early-1990s, the emphasis was not necessarily on solving accounting problems in considering new topics for the IASC institutional agenda. Instead the principal focus was on seeking recognition for the IASC's core standards by the International Organisation of Securities Commissions (IOSCO) and in ensuring the IASC's continuing relevance and authority as the recognised international standards setter (Camfferman and Zeff, 2007, Chapter 10).<sup>36</sup>

### **1.2.1 IASC Agriculture Steering Committee and Point Outline**

The project proposal in Appendix 7A placed Agriculture firmly in an international context. The IASC Board anticipated worldwide involvement on conforming existing and other proposed guidelines into the project; for example, there was a brief reference to *self-generating or regenerating assets* in para. 5 of the proposal not attributed to the AARF.

The Board approved an international SC to supervise the project. It was *'initially chaired by Narendra P. Sarada, from India, followed briefly by Hank Howarth from Canada, and from 1996 to 2000 by Reyaz Mihular, chairman of the Sri Lankan Accounting Standards Committee and a member of the India/Sri Lanka delegation'* (*ibid.*, p. 402). The SC initially comprised a representative from each of France, India, New Zealand, Thailand, Zimbabwe and the World Bank with its Project Manager, Ian Kirton, from New Zealand. SC membership over the Agriculture Project is summarised in Appendix 8B.

During 1995, the committee met twice to confirm the scope and conceptual framework for the project; to undertake and consider research individual country member bodies had already undertaken; all promulgations to date; how 'agriculture' was defined, the extent of any exclusions; examples of current reporting entity practice and identification of any issues member bodies considered ought to be covered by the SC. The aim was to prepare a project *Point Outline* to cover *'the recognition, measurement and disclosure of assets, liabilities, income and expenses resulting from growing crops, plantations and forestry, and livestock'* (IASC, 1996a, para. 1). This comment excluded bearer-assets; although para. 6 in Appendix 7A noted the more comprehensive Australian SGARA research study included *'agriculture, aquaculture, livestock, horticulture, viticulture and forestry'*.

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<sup>36</sup> IOSCO's core standards for the IASC excluded only IAS 40 *Investment Properties* and IAS 41 *Agriculture*.

As with the UNE in Australia, the SC sought to identify unique sector features in the context of an existing IASC accounting structure framework. This would help determine who the users might be and any of their special needs, the criteria for establishing a particular accounting model and the relevant disclosure requirements within the context of measurement, capital and capital maintenance classifications.

An early task was to define “Agriculture”. The working definition was the ‘*management of the biological transformation of animal and plant, to produce products for consumption or further processing*’ (*ibid.*, para. 16). The SC summarised ‘*biological transformation, the innate ability of biological assets, is the source of sector uniqueness*’ (para. 22).

Therefore the stance adopted by the SC was that any standard needed to be applicable to all agricultural systems and cover all biological assets as these represented agriculture’s distinguishing and dominant feature of ‘*transformative capability*’.

Having considered the various characteristics of the sector, users’ needs, the conceptual framework and an appropriate accounting model, the *Point Outline* concluded there was an urgent need for harmonisation of international accounting practice with focus upon recognition and measurement of biological transformation consistent with precedents already in place in other standards. Accordingly the SC proposed:

- adoption of a modified historical cost approach;
- assets for which modification was to be considered should be those biological assets unique to agriculture, and
- guidance would be sought from other Standards for any elements not falling within that classification’ (*ibid.*, para. 31).

The SC recognised this approach would need to combine with work already undertaken by the AARF for their *SGARA* project. Accordingly the committee ‘*would strive to ensure a synergy between the two projects*’ (*ibid.*, para. 22) to ensure expected inter-agency co-operation occurred amongst respective standard-setter agencies.

The principal conclusions and identified significant elements for further consideration in the *Point Outline* report included:

- a new standard should distinguish between the agricultural asset itself [*e.g.* a tree] and its product inventory [*i.e.* the fruit] in order to ‘*increase the potential for one proposed measurement method to apply to all biological assets*’ (*ibid.*, para. 61);
- future work on biological transformation needed to ensure reliability of transactional-based recognition and measurement methods during all biological transformation stages;
- the accounting recognition assumption should be that the primary source of economic benefits flow to the enterprise from holding tangible biological assets;
- the measurement criterion was an essential element. The accounting policy for biological assets had to conform to ‘*framework requirements of relevance and reliability, [but also] the biological growth event must be recognised*’ (para. 51). Historic cost, or any other cost-based method, might measure assets, but not biological growth. The SC acknowledged other ‘fair value’ alternatives were available in the IAS 16, *Property Plant & Equipment* and the evolving IAS 39 *Financial Instruments* standards. However, further consideration would need to be given to an overall valuation benchmark, such as market based exit- or entry-prices and expectation-NPV measurement methodologies; and finally
- in considering the unique characteristic of biological assets the committee would have to consider whether biological assets should be classified as inventory, fixed assets, or some other balance sheet classification; and whether sub-classifications were relevant such as for immature/mature or bearer/consumable categories.

The *Point Outline* proposal was submitted to the IASC Board in March 1996 as a restricted board paper. It is recorded in full in Appendix 7B.

The Board accepted the project formally onto its agenda and authorised commencement of work by the SC on the *Draft Statement of Principles for Agriculture* targeted for issue in November 1996.



### 1.3 Summary

The issue creation and agenda access processes and promotion to agenda entrance stages occurred from two entirely different perspectives. However the intention for each was to provide GPFR for Agriculture consistent with emerging conceptual frameworks.

In Australia, issue creation and agenda access were internal processes within the AARF. Initially it was primarily directed at remedying omissions in existing standards particularly for forestry and livestock, but extendible to other SGARAs.

The IASC followed three to four years later. Research had started earlier as an embryonic staff project specifically for developing and newly-developed countries, with external triggering signals received from the ECSAFA and ASEAN countries. The World Bank grant provided the funding impetus for agenda access to develop an agriculture standard for developing countries, but capable of general extension to agricultural sectors world-wide. Formal agenda entrance occurred on Board acceptance of the *Point Outline*. However, even at that early stage, misgivings were noted amongst some Board members.

The internally-generated processes were similar. Each had a detailed preliminary research design stage. In Australia, this was derived from the AARF internal *Project Brief*. The IASC first sought internal staff work on a project *Point Outline* for IASC Board approval. Some cross-referencing or co-operation would have occurred through Warren McGregor in his dual technical capacities between respective key insiders and Board decision-makers. Other formal or informal staff opportunities may have occurred during G4+1 meeting processes. But in this situation, development of a proposal was sometimes 'contracted out' to one agency rather than duplicated as was occurring for Agriculture. No discussion on G4+1 prioritisation was found in any IASC internal newsletters.

The preliminary issue creation, agenda access and agenda entrance stages were complete. The next agenda stage was formal work on and consideration of the Australian DP 23 *SGARA* Discussion Document and the IASC's *Draft Statement of Principles for Agriculture* in November 1996.

## Chapter 2. STATEMENTS OF PRINCIPLES

### Introduction

The Principles designed to under-pin the *Agriculture* standards were published in two different documents. Discussion Paper No. 23 for *Self-Generating and Regenerating Assets* (DP 23) was published by the AARF on behalf of its UNE contractor. The IASC Board required the steering committee (SC) to undertake further *Point Outline* research studies prior to agreeing to issue its *Draft Statement of Principles* (DSOP) on *Agriculture*.

Table 11 provides an overview for this rule-making agenda stage and process:

***Table 11. Agenda Statement of Principles Process for Agriculture***

<b>Rule-Making Stage</b>	<b>Elements</b>	<b>Modes of Lobbying</b>	<b>Evidence</b>
<b>Formal Consideration of Agenda Items</b>	AARF issues DP 23 IASC issues DSOP	Written submissions informal discussion	Written submissions, Journal & media articles.

Source: Table 9 further modified for *SGARA/Agriculture* standards processes.

This chapter considers the proposals contained in respective discussion memoranda, comparing the two where relevant. It also reviews evidence of internal and external political processes by or influences from the AASB and IASC gatekeepers in producing these discussion documents. Until then there had been no overt external involvement apart from the UNE and World Bank. There had been general concerns expressed about consistency of forestry accounting, GPFR exclusion of accounting for agriculture activities and initial indications a comprehensive standard may present conceptual and practical difficulties for some agricultural sectors.

The AARF published DP 23 in May 1995 and received only four responses. None were released publicly. This may have been because DP 23 was considered only a working document with several important areas requiring further research. The AARF had already decided to conduct that research on its own initiative.

The IASC issued its DSOP in December 1996. There were 42 written submissions. These were primarily from other standard-setter agencies confirming the IASC's initiative to develop a new standard but some respondents expressed minor reservations about the details.

## **2.1 Australia – Draft DP 23 Principles and Recommendations**

The initial public origin of the putative SGARA financial reporting system was contained in the AARF's SGARA Discussion Paper, No. DP 23 (Roberts *et al.*, 1995).

The purpose of DP 23 was to be *'part of the due process for formulating accounting standards in respect of self-generating and regenerating assets...such as forests, livestock and similar regenerative natural resources which were then specifically excluded'* from prevailing standards (*ibid.*, p. 1). The intention was to overcome the diversity in reporting practice *'with respect to the recognition, display and measurement of information about SGARAs in general purpose financial reports...[suggesting] a separate "industry specific" standard is required'* (p. 2).

DP 23 aimed to stimulate debate. Any *'official position could only be determined after extensive due process and deliberation, to which this Paper has not been subjected'* (*ibid.*, p. 1). It was a working research document. Apart from four submissions, that debate was to occur two years later with responses to the AASB's Exposure Draft, ED 83.

As noted, DP 23 evolved out of earlier UNE published work papers as an extrapolation from the two specific sectors of prime interest; being forestry (foremost) and livestock. These were described as SGARAs representative of the agricultural sector. However DP 23 acknowledged more research was necessary for other agricultural sectors.

DP 23 focus was on general purpose financial reporting consistent with the developing Accounting Concepts. With a certain circularity of logic *'the scope of the paper is determined by the definition adopted for SGARAs. The term "assets" in the phrase "self-generating and regenerating assets" implies that SGARAs are a particular type of asset'* (*ibid.*, p. 2) and, for the purposes of DP 23, SGARAs were defined as *'non-human-related living assets...[so that DP 23]...addresses the financial reporting issues which arise out of accounting for SGARAs which satisfy the broad definition of "assets"'* (p. 3). The distinguishing characteristic was living assets, not inanimate or intangible assets; although the *Project Brief* envisaged consideration also be given to measurement bases for intangible assets used in conjunction with SGARAs, refer [Appendix 6](#), p.16, para 4.B.ii.

### **2.1.1 The DP 23 Classification Approach**

DP 23 identified the *'plant/animal dichotomy'* as a common useful means of SGARA classification. No reference was found to support this. Indeed, in New Zealand, approved NZSA guidelines were established for most individual agricultural sectors.

The fundamental nature of SGARAs was described as: *'the natural capacity to grow and/or procreate. It is the physical change (both in quality and quantity) which is economically important'* (*ibid.*, p. 11); that is, its transformative capability whether because of growth, maturation or decline; or through reproduction, or by yielding produce from the SGARA asset itself.

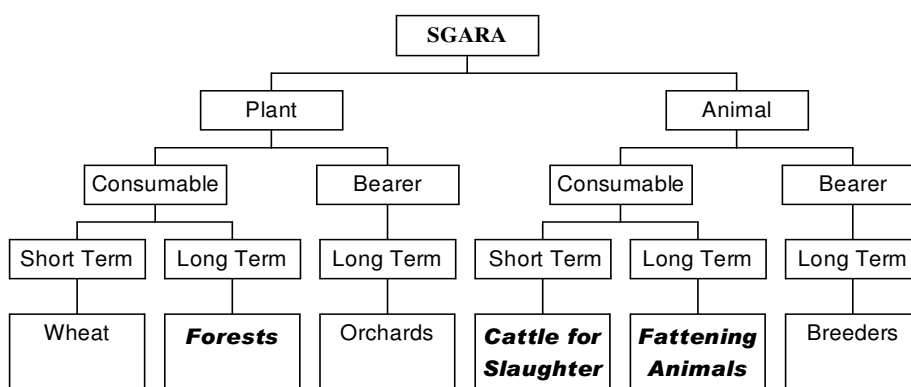
However, DP 23 claimed, surprisingly, that within that dichotomy *'forestry is representative of the plant category and livestock is representative of the animal category. It is therefore anticipated that the conclusions...in relation to forestry and livestock will be applicable to all SGARAs'* (*ibid.*, p. 4) [N.B. Emphasis added] so that *'discussion of the financial reporting issues relating to SGARAs is primarily made in the context of [these] two SGARA-related industries, forestry and livestock'* (p. 5). This formed the basis for evolution of the Australian standard – subject to further research being undertaken on the impact on other sectors. That was never carried out; or, if it were, it remains unreported.

### **2.1.2 DP 23 SGARA Biological Taxonomy Model**

The objective of GPFR was to *'provide information useful to users for making and evaluating decisions about the allocation of scarce resources'* (AARF, 1990b, para. 43). Thus information in financial reports should convey underlying economic attributes consistent with that objective. Continuing with the plant/animal dichotomy, DP 23 suggested:

at the simplest level, [the] distinction can be made between those SGARAs whose fundamental biological classifications are either plant or animal. This distinction is useful because the economic attributes, and therefore the risks and potential returns associated with each biological type of SGARA differ. Further, the plant/animal dichotomy is a generally accepted classification for SGARAs in the relevant literature. The Figure below displays the extended economic taxonomy for SGARAs and provides examples (Roberts *et al.*, 1995, p. 18).

Figure 3. - Economic Taxonomy For SGARA



Source: DP 23 (Roberts *et al.*, 1995), Table 2, p. 19.

Emphasis is added in **bold** to highlight the DP 23 plant/animal positioning for forestry and livestock. ‘Forests’ were identified as a long-term ‘Plant Consumable’ and ‘Cattle/Animals’ as either a short- or long-term ‘Animal Consumable’ respectively.

Reinforcing the earlier UNE Work Paper No. 2, DP 23 noted for GPFR purposes:

this taxonomy also appears extendible into the existing financial reporting classifications and descriptions of “current”, “non-current”, “inventory” and “plant and equipment”. DP 23 then considered whether it is useful to:

- describe SGARAs as either inventory or plant and equipment; or
- classify SGARAs as either current or non-current assets (p. 19).

It concluded this classification distinction has particular relevance for livestock since different economic benefits may occur throughout an animal’s life due to growth, reproduction or as produce. Management intent may also alter due to changing markets and environmental conditions. Therefore, given the ‘unique’ status of SGARAs, and to separate them from other assets, comparability across the sector is best achieved by establishing a separate balance sheet asset reporting classification for SGARAs.

In developing the earlier WP No. 2 discussion, DP 23 introduced further classifications:

SGARAs can be distinguished on the basis of whether they produce consumables once and then terminate their service potential or future economic benefits, or whether they produce consumables on an ongoing basis and thus retain their service potential or future economic benefits for an extended period of time.

In economic terms, SGARAs of the former type are often described as consumables. This is analogous to the financial reporting description of “inventory”. In economic terms, the latter type of SGARAs may be described as “durables”. However, this is a misnomer for assets, which, in the next period, can revert to a consumable. The classification “bearers” may therefore be more appropriate as it connotes a productive process leading to separable

products, e.g. eggs, offspring, fruit and wool. This description “bearers” is analogous to the financial reporting description “equipment” or “productive plant”.

It is therefore possible to describe SGARAs as either “inventory” or “plant and equipment” and thus comply with traditional balance sheet line item descriptions. However, such descriptions may not be adequate to capture the biological and economic nature of SGARAs and thereby communicate that nature to users of financial reports. For this reason, descriptions based on the taxonomy in the above [Figure] may be more appropriate. (p. 20).

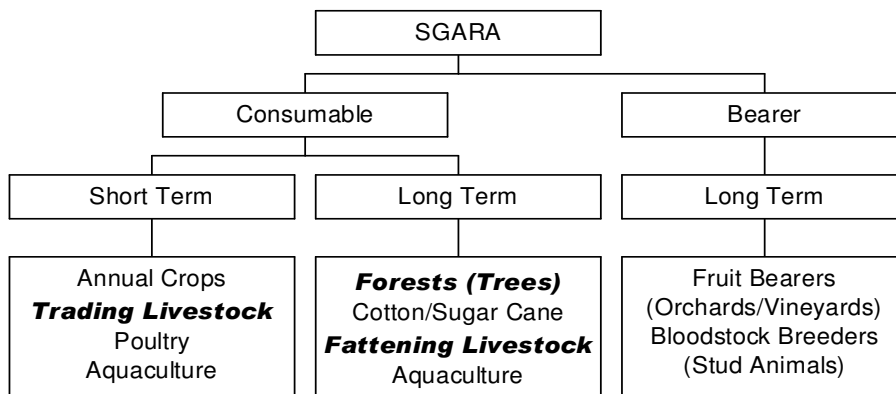
Further examination is warranted on the reasons DP 23 preferred the biological classification option compared to an underlying economic functional basis, especially given the GPFR preamble. This is also critical for later analysis of public submissions, and academic commentaries and other lobbying processes on succeeding Exposure Drafts and experience found with the eventual *Agriculture* standards themselves.

**2.1.3 Alternative SGARA Economic Functional Taxonomy**

Whilst the definitional basis for SAC 2 GPFR was described as emphasising economic attributes, the DP 23 text considered the economic attribute, but opted instead for the biological plant/animal dichotomy. Therefore the counter-factual interpretation should test the taxonomy and standard-setting recommendations on SGARA’s economic rather than biological functional classification; that is, on whether the SGARA classification should be for consumable and bearer categories instead of the plant/animal dichotomy.

The DP 23 taxonomy can be re-arranged to reflect SGARAs’ economic functionality:

Figure 4. Revised Economic Taxonomy For SGARA



Source: Figure 3 re-arranged for economic taxonomy classification.

Figure 4 separates long term non-current assets between the *consumable* and *bearer* economic functions. This functional classification is analogous to the principles previously identified in Section 3 for New Zealand's TPA-5 *Accounting for Livestock* (ARSB, 1986) and TPA-7 *Accounting for Bloodstock Enterprises* (ARSB, 1988) with their accounting treatment following economic substance rather than biological form.

Closer investigation of the template raises the question of whether the DP 23 bolded forestry and livestock categories were indeed representative of the whole. Both are more properly described as *consumables*, ultimately becoming 'inventory' on ceasing to be a SGARA when felled as lumber, or sold as livestock.

The extrapolation from these specific 'consumable sectors' to the whole of general agricultural accounting meant that a bearer-asset was deemed to be the equivalent of a consumable-asset whereas in reality, as DP 23 acknowledged, it is the produce of the bearer-asset which is the 'consumable'. Thus the DP 23 analysis excluded consideration of any accounting principles applicable to long-term bearer-SGARAs *per se*. Instead, further research was required for those other sectors, including for bearer-SGARAs, as described in Appendix 9.

Consideration of different accounting treatment is appropriate for the bearer-asset itself. For some livestock, an animal might be held either as 'consumable' inventory held-for-sale or, alternatively, held as bearer capital stock for its produce yield, such as progeny, wool or milk depending on its management regime or changed economic prices and circumstances.

A further clarification is also necessary when considering the taxonomy. Use of collective terms, *e.g.* 'forests' or 'animals', can be misleading. Technically, it is the individual SGARA itself, the animal or the tree that is relevant. However, in large scale commercial operations, SGARAs can be aggregated into age-classes within a herd, or as a unit age-class or stand within a forest or as a vine-varietal type within a vineyard. Reference to a forest as an aggregate collective, instead of the 'unit stand' concept, taken to its logical conclusion led to the development of *sustainable yield or perpetual* forestry accounting rules in New Zealand.

#### **2.1.4 Consumable- and Bearer-SGARAs**

The principal new features in the eventual *SGARA/Agriculture* standards were the introduction of market-based fair values for SGARA assets and produce, the manner of their reporting and the biological emphasis in an omnibus standard lacking differentiation between ‘consumable’ and ‘bearer’ economic functionality.

The *Project Brief* and UNE work had focussed upon the living characteristics of SGARAs, but not how their monetary properties were to be accounted. In that respect, for reporting purposes, SGARAs were no different to other tangible or intangible assets.

Two separate sector accounting rules could have been developed for each of the ‘bearer’ and ‘consumable’ economic functional classifications within AASB 1037 and later in IAS 41, as many submissions, and later the AASB itself was to recommend.<sup>37</sup> Had respective SGARA-types been accounted for and reported in monetary terms, like for any other assets, then virtually all objections to the new agriculture standards might have disappeared.

Moreover, had this occurred, analysis and consideration could have focussed upon more relevant issues for SGARA accounting. These could have comprised appropriate asset valuation measurement techniques, reliable accounting treatments for recognition and reporting of inventories, period income and performance, whether realised or unrealised, and relevant recommended disclosures for general purpose financial reporting.

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<sup>37</sup> In November 2003, as a result of its PIR survey and discussed further in [Section 6](#) below.



### **2.1.5 DP 23 SGARA - Recommendations**

The following sections summarise:

- the recommended DP 23 basic principles and whether and in what manner these were reflected in the eventual AASB 1037 *SGARA* standard; with the proviso
- DP 23 recommended further research and cost/benefit analyses be undertaken to validate the recommendations across all agricultural sectors.

#### **2.1.5.A. Basic Principles for SGARA Accounting**

As the first to recommend a new *SGARA* accounting method, DP 23 and the AARF obtained first-mover advantage in defining the proposed framework but at the cost of adverse criticism when their analyses were later disputed.

The DP 23 recommendations were stated as applicable to all *SGARAs*:

although it is acknowledged that practical considerations may lead to some recommendations being modified for certain *SGARAs*, particularly those with a short term production cycle. To the extent that the recommendations differ from the requirements of existing accounting standards, DP 23 recommends that those standards be amended (Roberts *et al.*, 1995, p. 89).

DP 23 reinforced their earlier comments on biological *SGARA* classification as:

the nexus between such generic terms as “bearer”, “breeding”, “trading stock”, “short term”, “long term” and “consumable” and the financial classification of “current”, non-current”, “plant” and “stock” is by no means clear. The problem is that one *SGARA* can possess more than one element. It can be both breeding and trading stock, both plant and equipment, and inventory; it can fluctuate between short-term and long-term; it can move from current to non-current and back simply because it is by nature changeable...[thus there is] a tenuous nature of any sub-categorisation of *SGARAs*, other than by type [*i.e.* forests and livestock] (*ibid.*, p. 89).

With this *caveat*, DP 23 provided each of its in-principle recommendations:

**Recommendation 1. Classification of SGARAs**

*SGARAs should be reported as ‘Self-Generating and Regenerating Assets’ as a category separate from current assets and non-current assets and identified by sub-categories or types of SGARAs, such as plants and animals. These types should be further classified in accordance with the economic taxonomy presented [as shown above] in Figure 3 (ibid., p. 90).*

The justification for the separate category was the variety of reporting experiences found by UNE research. UNE sought responses from 76 SGARA entities, but only 17 replied. Roberts *et al.* also reviewed six state-owned forestry entities - covering over one-half of Australia’s naturally occurring forests and two-thirds of planted forests - and also selected five major private-sector companies controlling about one-half of all privately owned forests. For livestock, they reviewed nine private-sector reporting entities.

DP 23 referred to the low response rate. There was a partial qualification supplied:

the findings are anecdotal in nature. However because the discussion...relates to all SGARAs (using forestry and livestock as a vehicle for discussion) the lack of empirical evidence from which conclusions may be drawn in relation to SGARAs other than forestry and livestock is not considered to be a limitation (*sic*) rather, the extent to which anecdotal evidence is derived by the research provides insight into possible practical issues which may be encountered in financial reporting for SGARAs generally (*ibid.*, p. 90).

Having identified the UNE research was not comprehensive, DP 23 returned to the principal objective to standardise forestry accounting and ensure reporting consistency between entities. This could then be extended to all agricultural sectors.

DP 23 proposed a balance sheet SGARA asset category separate from current- and non-current assets because of SGARA’s special characteristics.

However, the eventual AASB 1037 *SGARA* standard discarded this recommendation. Instead SGARAs were to be identified separately within whichever current- or non-current asset reporting category the preparer determined appropriate, with fulsome note disclosures. This change in AASB 1037 may also have reflected a realistic assessment that a separate, unique SGARA balance sheet asset classification implied a departure from presentational requirements in Australia’s Corporations Law. Subsequently the eventual IAS 41 Agriculture standard also followed the AASB 1037 reporting basis.

**Recommendation 2. Measurement of SGARAs**

*It is recommended that a valuation method should be adopted for SGARAs that best estimates the current market value of the assets. There are alternative views as to whether entry prices or exit prices should be used in identifying current market value. It is recommended that this issue be resolved in the context of the more general question of the measurement of all assets and liabilities. In the absence of reliable current market prices, an appropriate surrogate for current market value should be adopted (ibid., p. 90).*

Fully one-half of the DP 23 Report discussed measurement principles in the context of the emerging Statement of Concepts in support of this recommendation. [Appendix 9](#) contains all the alternative forestry and livestock sector valuation measurement methods considered and, for the record, summary cross references for each within the DP 23 Report.

DP 23 preferred the capital maintenance concept, represented by asset replacement at ‘entry prices’ as the appropriate current market value (CMV) measurement basis for some purposes, and for other purposes, the current market price alternative with ‘exit-prices’ expressed as representative of CMV.

The preference for a current exit-price market value was based upon a presumed ‘*ready availability of market prices, thus facilitating the practical application of the current market value method*’ (ibid., p. 45). Whilst that may be applicable for a short-term consumable-SGARA, it was not necessarily satisfactory for periodic measurement recognition of forest assets over their full maturation period, or for bearer-SGARAs.

DP 23 acknowledged exit-price market values may not always be discoverable. Accordingly, it was necessary to develop other valuation surrogates, such as net present value (NPV) – even though for GPFR inter-entity comparison purposes there will always be variations between resulting asset values due to differing NPV component assumptions, calculation bases and discount rates.

This was therefore only a partial solution without a recommendation on a proposed ranked valuation hierarchy, since CMV may be an entry- or exit-price valuation, or a surrogate.

### **Recommendation 3. Recognition and Measurement of Revenue from SGARAs**

*Any increment/decrement in the current market value, or surrogate thereof, of SGARAs be separated into that which is due to volume or physical changes and that which is due to price changes. For the increment/decrement in value due to volume or physical changes, it is recommended that it be recognised as revenue/expense in the profit and loss or other operating statement in the relevant period. For the increment/decrement in value due to price changes, in the context of maintaining productive capacity, it is recommended that it be recognised as a capital maintenance adjustment in an appropriate reserve (ibid., p. 91).*

DP 23 elaborated at length on this recommendation. By their definition, physical growth or transformation was the distinguishing feature for a SGARA compared to any other type of asset. Underlying the discussion was the productive capacity concept of capital which was described as *'the appropriate concept in relation to SGARAs'* (ibid., p. 47). In New Zealand, TPA-7 had already recognised this for bearer breeding livestock (ARSB, 1988) and the IASC's DSOP was also to recommend this approach in December 1996.

The recommendation to dis-aggregate carrying value changes into separate price and volume change components was not subsequently adopted in either of the AARF's Exposure Draft ED 83, or in the IASC's E65 Exposure Draft. Instead, as a material new proposal, the entire combined value change in net market values during the accounting period was to be recognised as revenue or expense within the income statement.

In promoting this alternative to DP 23, the AARF noted in its Exposure Draft discussion that it may be impractical to separate the change in carrying amount into its price and biological components without making an arbitrary allocation. However Roberts, co-author of DP 23, was to make two submissions on ED 83 on this matter.<sup>38</sup> His submission referred to DP 23, Appendix 6, and claimed the two elements may be separated following sound accounting principles. The AARF objection failed to reflect traditional livestock accounting recognition whereby biological age and numbers were commonly, and reliably, differentiated from livestock price changes.

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<sup>38</sup> Roberts was later also to make a submission on these and related matters on each of the IASC's DSOP and E65, and a separate submission on the AASB's PIR in 2003.

**Recommendation 4. Disclosure of Non-Financial Information**

*SGARAs should be disclosed in general purpose financial reports with sufficient description in non-financial terms for the user to identify the types of SGARAs controlled by an entity and their relative quantities and qualities, and the nature of any externally-imposed restrictions thereon. It is also recommended that disclosure be made of the extent to which losses arising from natural events are insured, and that some specific form of geographic segment information be disclosed to allow users to assess the risks attached to SGARA holdings. Further, the accounting profession is encouraged to seek to play a role in assisting the development of the increasingly important area of accountability relating to environmental accounting (ibid., p. 92).*

DP 23 developed the case for specific GPFR non-financial and supplementary SGARA-related disclosures – but without any associated cost/benefit analysis in support. Their discussion concentrated on forestry and public-entity sectors but also referred to the fishing industry. Wherever possible ‘*market values of public resources should be adopted for financial reporting purpose...however, substantial difficulties will arise in determining net market value, or a surrogate thereof, because markets may not exist or are otherwise unreliable reflections of scarcity value*’, e.g. when valuing natural forests (*ibid.*, p. 85).

The reference to environmental accounting is beyond the scope of this study, but was of particular interest to Herbohn *et al.* (1998).

**Recommendation 5. Biotechnology**

*Further research is required into financial reporting issues which relate to biotechnological assets (ibid., p. 92).*

Biotechnology was one of the SGARA Other-industry segments discussed in [Appendix 9](#), p. 48, where further research was deemed necessary into financial reporting implications for biotechnological assets and the way such assets should be recognised. It was acknowledged, as a possibility, that further research might conclude biotechnology lay beyond the scope of DP 23.

### **2.1.5.B. Further Research Indicated by DP 23**

DP 23 also considered some of the other non-forestry and livestock industry sectors. These were Consumable Crops; Fruit Bearers: Orchards and Vineyards; Aquaculture and Fishing Consumables, Stud Breeders; and Biotechnology. The commentary is of historical interest and is summarised in [Appendix 9](#).

There was no research or cost-benefit analyses reported for these sectors or any other analytical criteria to support the recommendation to extrapolate forestry and livestock *SGARA* accounting to these sectors (*ibid.*, pp. 73-81).

However DP 23 provided two general observations in respect of these other sectors:

- there was a wide range of reporting practices for these industries, as with forestry and livestock. Some entities adhered to existing reporting standards, even though agricultural assets and produce were explicitly excluded, whilst others simply ignored them; for instance, by adopting tax or other standard value bases; and
- even with diverse accounting practices:
  - the fundamental self-generative and regenerative characteristics of all *SGARAs* means the principles developed for forestry and livestock can be applied to all *SGARAs*. However, as indicated, the costs and benefits of applying such principles need to be considered, particularly in relation to those *SGARAs* with a short-term production cycle (*ibid.*, pp. 80-81).

Independently, the AARF decided to conduct that further research itself. One result, whether intended or not, was that the AARF gatekeepers remained in control of the on-going development of the standard for subsequent rule-making stages.

Funding for this research was provided from a separate Government-sponsored Rural Industries Research and Development Corporation grant (RIRDC, 1999, Sept.). The agreed objective was to develop a more general accounting standard applicable to all *SGARAs*. This is examined in the next chapter (on pp. 134-5) and in [Appendix 12](#).

## 2.2 AARF Consideration of DP 23 and Submissions

Discussion Paper No. 23 was formally released in May 1995 (Roberts *et al.*, 1995). As noted, the AARF received four submissions.

The *Project Brief* indicated a Project Advisory Panel would be appointed to assist AARF staff, under Robert Keys, the AARF Senior Project Director. The purpose of the panel discussion on 19 October 1995 was to consider a Key Decisions Questionnaire (KDQ) based upon the five DP 23 Recommendations and to agree a strategy to inform the AASB Board of developments at a future Board meeting.<sup>39</sup>

The Panel comprised representatives solely from the forestry sector, although Russell Philp also had family interests in cattle grazing.

***Table 12. AARF SGARA Project Advisory Panel Membership***

Panel Member	Organisation
K. Felton	Forestry Tasmania
P. J. Johnston	Bunnings Limited
B.M. Macdermott	North Forest Products Limited
R. Philp	CSR Limited
Ms K. Robinson	Northern Territory Treasury
D. Riddell	Forestry Tasmania
G. Bradley	Queensland Treasury

Source: AARF Support Papers for KDQ Panellists, ex J.J. Staunton's papers.

The Panel considered the four submissions. Each related to forestry. Two were from *Forestry Tasmania*, including one from panellist Ken Felton; one was from the *Queensland Department of Housing: Local Government and Planning* which identified a lack of any DP 23 discussion, or current consensus on accounting treatment for non-commercial ornamental, road-side and botanical-garden mature or rare trees all of which met the DP 23 SGARA definition. The final submission was from the *Queensland Treasury* which provided an outline of its NPV surrogate 'net realisable value' valuation approach for the State's plantation forest assets.

<sup>39</sup> Contained as attachments to Agenda Item 4f - 'SGARAs KDQ' Memorandum. The agenda, notes and discussion topics were derived from papers kindly supplied to the writer by Dr. John (J.J.) Staunton.

The discussion process followed each of the DP 23 recommendations. A feature was the formal guidance and apparent activist stance taken by Robert Keys, and AARF staff, in considering each of the topics and when summarising panellists' views for a consensus. This can be interpreted as influencing the criteria for and outcome of debate with panellists to obtain a conformed view for the proposed exposure draft. At the time, this was planned for publication six months later, in the first half of 1996.

### **2.2.1 Need for a Standard**

Not surprisingly, the conclusion was the *'to continue [the] project of developing a Standard for SGARAs and staff should continue to provide assistance to, and monitor the work of, the IASC's Agriculture Steering Committee'*.

The reasons cited included the economic significance of agriculture, especially forestry, to the Australian economy; the diversity of accounting practice; the "A" high priority rating given by the State Treasuries Liaison Board and the third highest priority from the PSASB; the perceived support especially from the States and the Forestry Sector; and that the IASC had the previous year included an *Agriculture* project on its work programme.

Contrary arguments expressed by staff, in discussion, were that Australia should not *'lead the world in promulgating standards'*. The majority of SGARA producers were not GPFR reporting entities and SGARAs were no different to other assets. Therefore accounting principles for other assets should apply equally to them – even if specifically excluded by existing standards.

### **2.2.2 Scope of the Standard**

The meeting considered how to define SGARAs. The choices were to accept the DP 23 definition of *non-human-related living assets*; to adopt the definition contained in existing standards, which excluded SGARAs as *forests, livestock or similar regenerative assets*; or, to define SGARAs in some other way.



The discussion noted recommendations in DP 23 relating to short-term production cycle SGARAs and advances in biotechnology. The panel addressed questions raised in the four submissions, *e.g.* from Forestry Tasmania - whether the new standard should be extended to address accounting issues relevant to all forestry assets and not just forestry SGARAs, and from Queensland Department of Housing – whether or not to include ornamental trees.

In summary, the staff view was that the recommended DP 23 definition of SGARAs be retained to define the scope of the standard, and that explanatory guidelines be sufficiently inclusive to cover ornamental trees, short production cycle and biotechnology SGARAs.

### 2.2.3 Measurement of SGARAs

The staff's Key Issues paper questioned whether measurement should be Cost-Based or Value-Based; and, if the latter, whether Net Present Value or Current Market Value.

This was a major component of the DP 23 Report which had discussed in detail the relative merits of each. The staff paper reflected the DP 23 argument that *'a value-based method is preferred to a cost-based method as the resultant financial information is more relevant by recognising the value of biological change which occurs uniquely in SGARAs supplemented by equivalent developments occurring elsewhere overseas'*. This latter reference inferred staff had some knowledge about concurrent work within the IASC, presumably supplied by Warren McGregor.

However panel members and submitters provided differing views. Table 13 distils views recorded in the meeting notes:

***Table 13. SGARA Measurement Evaluation by Advisory Panellists***

<b>Panel Member</b>	<b>Organisation</b>	<b>Cost or Value</b>	<b>Preferred Value Method</b>
K. Felton	Forestry Tasmania	Value-based	Net market value
P. J. Johnston	Bunnings Ltd.	Cost-based	Cost but disclose value-base
B.M. Macdermott	North Forest Products Ltd.	Value-based	NPV of net cash flows
R. Philp	CSR Ltd.	Cost-based	
Ms K. Robinson	Northern Territory Treasury	Value-based	Current Market Value (CMV)
D. Riddell	Forestry Tasmania	Value-based	Market value, or surrogate NPV
G. Bradley	Queensland Treasury	Value-based	Market value, or surrogate NPV

Source: AARF Support Papers for KDQ Panellists, ex J.J. Staunton's private papers.

Adoption of a recommended valuation basis needed resolution of some related issues:

- to identify whether market pricing reflected an immediately available market or the intended actual market. DP 23 preferred the latter; however,
- if NPV were identified as the valuation method, or as a CMV surrogate, guidance was needed on the appropriate discount rate to be used; whether entity-specific, per DP 23, or a current investment market rate;
- if CMV were prescribed, would it be as an entry-price or an exit-price; and
- if CMV were applicable, what would be the exit-proceeds recognition basis for the non-living produce when measured in a cost-based inventory accounting standard.

The staff view addressed these issues as follows:

- a CMV value-based method should be prescribed as it recognises the value of biological change and avoids the subjectivity involved in the NPV method;
- the standard should provide guidance on identifying the appropriate intended market, to which reference should be made for determining market value;
- the standard should also acknowledge that, in certain circumstances, CMV may not be available for SGARAs and therefore a surrogate should be adopted;
- the standard should provide guidance on possible surrogates and, if NPV is accepted as the surrogate, guidance given on selecting an appropriate discount rate, that is, an entity-specific rate as a surrogate or an asset-specific rate should be provided; and
- the standard should provide guidance on the measurement of the non-living product of SGARAs.<sup>40</sup>

These measurement issues were fundamental. Standard-setter views were to change as rule-making stages progressed.

In Table 13 most panellists preferred a current market value (CMV) basis leaving the third measurement KDQ surrogate as entry-price (*i.e.* current replacement cost) or exit-price (*i.e.* net market value). DP 23 was not definitive. In practical terms, where market prices were not readily observable a surrogate was required anyway so entry- vs. exit-prices was less relevant. Roberts *et al.* (1995) had argued the difference would not be significant if the difference between the two represented transaction costs.

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<sup>40</sup> From Staunton private papers; *op. cit.*, p. 11.

The staff view was that in conceptual terms this was insufficient. A selection was required as to how changes in value were to be recognised. DP 23 had concluded '*it is recommended this issue be resolved in the context of the more general question of the measurement of all assets and liabilities*' (Roberts *et al.*, 1995, p. 90).

Riddell, from Forestry Tasmania, recorded that NMV, *i.e.* an exit-price, was equivalent to CMV. He regarded CMV as unworkable. Therefore there was no need to choose between the two if an NMV basis were adopted. These comments emphasised staff attention given to supplying a standard suitable for forestry. Trading livestock always had reference market prices available from livestock auctions or current price schedules.

AARF staff focussed upon developing a general SGARA standard consistent with other projects. At the time AARF was working on a draft *Accounting Theory Monograph 'Measurement of Accounting'* (later issued as AARF, 1998a) which was noted in the KDQ memorandum as containing Keys' conclusion, as AARF Project Director, that:

a 'Relative Current Value' system is the preferred system for measuring all assets and liabilities. This system entails a 'value to the entity' basis of asset value and is therefore consistent with what is referred to as entry prices in DP 23.<sup>41</sup>

DP 23 had concluded that existing and emerging accounting models like deprival value and SAP 1 *Current Cost Accounting* were consistent with adopting an entry-price valuation for SGARA entities, as elaborated in Appendix 5, DP 23 (Roberts *et al.*, 1995).

The difficulty identified was that current conceptual models included a recoverable amount 'impairment' test. Therefore NMV measured at exit-prices, or its NPV surrogate, can be less than current replacement entry prices, even excluding any transaction costs.

In summary, the staff view expressed to panellists appeared to be that if NMV were less than an entry price, no write down should occur:

- consistent with Statement of Accounting Practice SAP 1 'Current Cost Accounting' and the deprival value model, entry-prices should be adopted for SGARAs;
- a recoverable-amount test should be applied to SGARAs...but this would not need to be re-expressed in the context of the valuation methodology proposed as, for example, it may be inappropriate to write SGARAs down to NMV, where it is used as a reliable measure of recoverable amount, if those assets would be replaced.

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<sup>41</sup> From Staunton papers, *op. cit.*, p. 13.

### 2.2.4 Revenue Recognition

On the basis a CMV approach were adopted:

there was a further need to consider the capital maintenance alternatives of:

- the financial concept, *i.e.* CMV change of SGARA's carrying values recorded as revenue/expense in the income statement; or
- the physical concept, *i.e.* the biological change to revenue/expense and the remaining balance attributable to price change be credited as a capital maintenance adjustment in reserves within the statement of non-operating movements in equity (SONOME).

DP 23 had concluded the physical concept was most relevant for SGARA entities. Recorded comments were confined to Ms K. Robinson, who supported CMV as the appropriate revenue concept, whereas Bradley, from Queensland Treasury, suggested all unrealised value movements, whether volume- or price-related, should be recognised in reserves with supplementary disclosures of respective movements during the period.

The list of discussion issues prepared by staff concentrated on SGARA's unique biological transformative attributes. However any value change treatment, attributable to price changes, should be treated identically to all other asset classes.

Existing standards required price change recognition through a revaluation reserve, except for certain financial assets. Keys' draft *Measurement of Accounting Monograph* concluded in favour of the current general purchasing power of capital as the appropriate capital maintenance concept. As such, biological changes and specific asset price changes would be recognised within revenue whilst the capital maintenance adjustment for changes in general price levels would be credited through reserves in SONOME.

However, there were immediate issues identified with dis-aggregating CMV movements into price and biological components. Panellists suggested the cost of determining the correct split might exceed any benefits. Bradley suggested, radically for an internally-developed project, that the implications should be tested with industry participants to determine what was practical.

The staff view recorded current AARF thinking:

- a change in CMV attributable to biological change should be recognised as revenue/expense. At a conceptual level, the current thinking of staff is that the change in CMV attributable to price change should be recognised as a capital maintenance adjustment. This view is consistent with adopting entry prices;
- however staff acknowledge that adopting such a view in Australia may be perceived as moving ahead of other jurisdictions, where measurement concepts have not been prescribed;
- staff are also conscious of the view that a physical concept of capital maintenance for SGARAs should not be adopted in the absence of the Australian standard setters finalising their ‘measurement project’; furthermore
- practical issues may arise from segregating CMV movements...[so staff] should continue to seek input from practitioners and other interested parties on the practicalities of segregating value changes due to price changes and biological changes.<sup>42</sup>

### 2.2.5 Presentation

The key issues identified were whether the DP 23 recommendation for a *Self-Generating and Regenerating Asset* category should be disclosed separately from current- and non-current assets and identified by types of SGARAs, such as plants and animals. Alternatively, should these to be further differentiated either as current- or non-current assets, or included within Property, Plant and Equipment (PP&E), or Inventories, with SGARA sub-classifications.

Current Forestry practice was noted as variable between PP&E, as ‘Fixed and Non-current Assets’, and with a wide variety of different types of forestry descriptions. Livestock experience was mixed between current- and non-current Inventories with varying descriptors for different types of livestock.

At the 19 October 1995 meeting, panellists did not reach a conformed position.<sup>43</sup>

As noted, the staff view was that ‘*SGARAs should be reported as “Self-Generating and Regenerating Assets” as a category separate from current and non-current assets and identified by sub-categories or types of SGARAs, such as plants and animals.*’<sup>44</sup>

<sup>42</sup> From Staunton Papers; *op. cit.*, p. 15.

<sup>43</sup> There was no reference in Staunton Papers to any subsequent Advisory Panel meeting.

<sup>44</sup> Staunton Papers, p. 17.

### **2.3 IASC – Pre-Exposure Draft ‘Principles’ Agenda Process**

During the early 1990s the IASC Board and staff had been working under time pressure from IOSCO to develop the agreed ‘Core Standards’ project so that IOSCO could endorse the full suite of international accounting standards to the U.S. Securities and Exchange Commission.

Initially, in June 1994, *Agriculture* was included as a core standard. However internal pressure on the SC reduced when IOSCO agreed, in December 1996, that *Agriculture* need not be a core IASC project (IASC, 1996c). The project subsequently developed at a more ‘leisurely pace’ (Camfferman and Zeff, 2007, p. 402).

The SC project mandate was to produce a Draft Statement of Principles on Agriculture for wider publication. The purpose of a DSOP was to:

- set out arguments for and against the development of an International Accounting Standard on the topic;
- set out the accounting principles that will form the basis of an Exposure Draft of the proposed International Accounting Standard. The principles will be supported, where appropriate, by proposed implementation guidance; and
- describe the alternative solutions considered and the reasons for recommending their acceptance or rejection.<sup>45</sup>

The SC throughout the period from *Point Outline* development to DSOP publication comprised representatives of country accounting bodies being: Chairmen H D. Horwath (Canada), and M. Reyaz Milhular (Sri Lanka); I. F. Kirton - Project Manager (NZ); J. Allimant (France); J.A. Atkinson (Zimbabwe); Ms B. A. Monopoli (NZ); K. Narongdej (Thailand); A. Priebjrivat (Thailand); N.P. Sarda (India) and G. Russell (World Bank) – refer [Appendix 8B](#) - as well as observers represented by Koninklijk Nederlands Instituut van Registeraccountants, Wye College of the University of London and PACIOLI – a concerted action group for the European Commission (IASC, 1996b, p. 3; Camfferman and Zeff, 2007, p. 402).

The original DSOP development and publication timetable was nine months after acceptance of the *Point Outline*. This target was met. DSOP was issued in December

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<sup>45</sup> Refer [Appendix 7A](#), IASC Project Proposal, Draft Statement of Principles, para. 18. This was presented as Appendix 1 to Agenda Paper 9 for the IASC Board Meeting in Brussels, in March 1996.

1996 and approved for public comment. Ian Kirton as Project Manager then sought comments from interested organisations and individuals as required in the original brief.

However Camfferman and Zeff noted a shift in emphasis. Initially, the project arose from funding support by the World Bank for benefit of developing countries. The IASC's project *'proposal to the World Bank had made it clear that the IASC would seek to draft a standard that would be applicable to enterprises in all countries, yet it had also strongly emphasised the practical relevance of the project to developing countries.'* But, as had occurred in Australia, the emphasis had shifted to *'a challenge of a more intellectual nature, that is, to deal with the unique features of biological assets in a way that was consistent with the IASC's evolving interpretation of its own Framework'* (p. 402).

The full summary of Principles and Specific Questions sought against each is contained in [Appendix 10](#). Unlike the AARF's DP 23 process, the SC actively sought to determine whether respondents supported the 'principles' and 'guidance'; and if not, what changes were recommended. Reasons were sought for any suggested changes, together with any additional guidance considered necessary.

### **2.3.1 'Draft Statement of Principles' for Agriculture**

There were similarities in principles and accounting treatment between the Australian DP 23 and the IASC's DSOP.

In summary, the key DSOP proposals were:

- biological assets, and any resulting agricultural produce, should be measured at each balance date at their fair value, primarily net market value;
- the change in carrying amount of a group of biological assets should be allocated between:
  - the physical change in biological assets – reported in the income statement; and
  - changes in fair values – reported in a statement of non-owner movements in equity;
 and
- biological assets should be classified as neither current nor non-current' (IASB, 1997, March)

### 2.3.2 Need for a Standard

The SC provided an overview of project objectives: *'the main objective of the IASC was to develop International Accounting Standards that are relevant in the financial statements of all businesses in all countries'* (IASC, 1996b, para. 1). It acknowledged the rationale for World Bank sponsorship, *'the importance of agriculture in developing and newly industrialised countries and requests from other countries...have reinforced the need to consider an International Accounting Standard (IAS) on agriculture'* (para. 6).

As additional justification, the DSOP described the diversity of agricultural accounting treatment across jurisdictions and exclusions of agricultural activities from existing IAS.<sup>46</sup> Special characteristics included different forms of biological transformation. The worldwide importance of the agricultural sector, with some large reporting entities, required an IAS. But a special sector feature was the predominance of small- to medium-sized family units and entities not normally required to produce GPFR statements. It was considered important to create consistent accounting treatment for all agricultural entities.

The purpose was summarised as the recognition, measurement, presentation and disclosure of specific items for entities required to present general purpose financial statements (para. 8). The DSOP had to cater for each of these elements and provide guidance on special accounting for the diversity of agricultural activities to obtain uniformity of, and precision in, treatment of reporting financial performance within the whole agricultural sector (para. 10).

A key consideration was whether to accept the traditional 'historic cost' model or to pursue the precedents already contained in some standards by departing from that model. *'Provided the methods recommended demonstrate greater relevance, reliability, comparability and understandability the steering committee believes improvement and harmonisation will be served'* (para. 12).

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<sup>46</sup> Viz. IAS 2, *Inventories*; IAS 4, *Depreciation*, & IAS 16, *Property, Plant & Equipment*, each of which exclude forests and similar regenerative natural resources and IAS 18, *Revenue*, which excludes natural increase in herds and agricultural and forest products. Refer also [Appendix 1](#).



The DSOP traversed what constitutes biological, transformative and management characteristics (paras. 14-16) and reinforced the DP 23 position that biological transformation was the source of sector uniqueness. However a new feature was the discussion on ‘produce’ where the DSOP distinguished between:

**Biological assets**, groups of animals and plants held for their regenerative and self-generative abilities;

**Agricultural produce**, which is harvested and therefore non-living awaiting sale, consumption or processing; and

**Agricultural produce incorporated in further processing** in integrated agri-businesses which, not being unique to agriculture, are excluded from the DSOP scope (para. 17).

The DSOP provided an explanatory table which featured subsequently in modified form in the IASC E65 Exposure Draft and explanatory notes to the eventual IAS 41 standard.

*Table 14. IASC Agriculture Project - Biological Asset and Produce Examples*

<b>Agriculture</b>		<b>Agribusiness</b>
<b><i>Biological Asset</i></b>	<b><i>Agricultural Produce</i></b>	<b><i>Production Output</i></b>
Flock	Wool	Yarn/Carpet
Forest	Log	Timber/Pulp
Growing Crop	Wheat	Bread
Growing Crop	Cotton	Thread/Clothing
Herd	Milk	Cheese/Casein
Plantation	Cane	Sugar
Plantation	Latex	Rubber
Plantation	Leaf	Tea
Vineyard	Grape	Wine

Source: IASC DSOP, Table in para. 17, p. 18.

However, unlike DP 23, the DSOP acknowledged that accounting for management intent needs to be sufficiently flexible to change through time when market conditions changed.

Therefore the characteristics identified for the DSOP and within the Framework include:

- biological assets meeting the definition of tangible assets must be controlled by the entity and be a source of expected future economic benefits;
- biological assets meeting recognition criteria will have a value that can be measured reliably;
- biological transformation alters the substance of the assets and under the accrual system these significant events must be recognised as they occur; but
- biological transformation gives rise to a number of outcomes, each measurable and tangible, whereby the asset changes or a new asset is created. Any such outcome is traceable to common joint cost inputs but agricultural activities add to the complexity of

allocating inputs to outputs potentially impairing the degree of reliability, comparability and understandability; and thus

- the range of possible outcomes and lack of traceability necessitates a consistent basis of measurement if meaningful representations of current period performance are to be derived (para. 18).

On these bases, the SC developed the DSOP's 'principles' for accounting for the respective elements resulting from biological transformation; namely, for biological assets, agricultural produce and agricultural land.

### 2.3.3 Scope of the Standard

The SC summarised the Scope in Principles 1 and 2 (*ibid.*, paras. 20-33):

the principal issues in accounting for biological assets, timing of recognition of changes in assets, the determination of their carrying amounts, the determination and accounting treatment of accretions or impairments to the carrying amounts, and the presentation of these assets and asset changes in the financial statements (para. 29) and their most relevant and reliable measurement (para. 33).<sup>47</sup>

Given the earlier DP 23 discussion about the plant/animal dichotomy, represented by forests and livestock, the DSOP provided a broader definition and range of agricultural sector consumable and bearer types - probably reflecting the SC's more diverse geographic membership:

- **Consumable** activities in which the animals or plants themselves are to be harvested, for example, beef, ginseng, and forestry or annual crops such as maize, wheat and barley; and
- **Bearer** activities in which the animals or plants are to bear produce for harvest, *e.g.* tea, apples, rubber, goats for fibre or milk, or coppice firewood production (para. 26).

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<sup>47</sup> Refer also [Appendix 10](#) for IASC Draft Statement of Principles.

### 2.3.4 Measurement of Biological Assets

The key principles in the DSOP were that ‘*biological assets should be measured at each balance date at their fair value*’ (Principle 3) and ‘*the primary indicator of fair value should be net market value*’ (Principle 4) (*ibid.*, paras. 34-57).

The DSOP discussed the historic cost vs. current value methods before opting for the latter because of relevance and reliability. Whilst lifetime income for an asset may be the same under either method, different valuation methods alter the timing and incidence of income recognition through an asset’s life. The exemplar was a forest crop. Under the historic cost method no income was reported until first harvest, 20-30 years after planting.

However the current value method recognises and measures biological growth progressively; thereby increasing usefulness and assessing the current period financial performance and balance sheet position (para 37). Having preferred current value, the SC noted alternative precedents in other standards, *e.g.* for replacement cost in IAS 15 and IAS 22; net realisable value in IAS 2, and net present value, in IAS 15 and IAS 16.<sup>48</sup>

The SC distinguished between market value and the asset values attributable to future benefits implied in each of the precedents above. They did not necessarily equate to market value. The question was whether the alternatives would reflect current market value and were capable of independent verification in active and efficient markets.

Camfferman and Zeff (2007) noted ‘*fair value*’ was gaining acceptance in IASC standard-setting deliberations; *e.g.* in IAS 39 *Financial Instruments*, and later in IAS 40 *Investment Property*. This created a precedent for the *Agriculture* standard even though biological assets were non-monetary assets. However the SC advocated the proposed fair value approach had ‘*greater relevance, reliability, comparability, and understandability as a measure of future benefits expected from biological assets when compared to historical cost*’ (IASC, 1996b, para. 45).

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<sup>48</sup> IAS 15 *Information on the Effects of Changing Prices* [subsequently withdrawn]; IAS 22 *Business Combinations*, IAS 2 *Inventories* and IAS 16 *Property Plant & Equipment*.

The SC did consider, but rejected:

- a benchmark of fair value with an allowed alternative treatment of historical cost because of the
  - pervasiveness of biological transformation as an event or through time;
  - greater relevance and reliability achieved by a fair value system;
  - greater comparability and understandability achieved by mandatory fair valuation in the presence of active and efficient markets; and
  - simplicity achieved by a mandatory fair value system applied to all biological assets (para. 47).

However, the SC did recognise that markets may not always be active and efficient, nor share the geographic location of an entity's activities. Valuation surrogates may be required. For example, a most recent market price, prices for similar assets in the vicinity, or in markets elsewhere, sector benchmarks, net present value assessments – or, in some situations, cost, *e.g.* where there had been little biological growth or where price impact was immaterial. The committee also recognised that a bearer plant was attached to land so there would be no independent market value for the biological asset *per se*. Instead, only a derived value could be attributed (para. 55).

### **2.3.5 Measurement of Agricultural Produce**

The pivotal valuation measurement event for biological produce was at the point of harvest when the consumable biological asset ceases to be living or attached to a bearer asset. Whilst the 'asset or produce' is still living it should be measured at a market-based fair value at each balance date where the biological asset is itself valued at fair value. Any change in carrying value of produce between two balance dates should be recognised in the income statement (Principle 18). Agricultural produce harvested for processing activities within an integrated agri-business should be valued at fair value as at the date of harvest – and this amount should become the 'deemed cost' for inventory valuation purposes under IAS 2 (Principle 19).

This was a contentious issue. For instance, it conflicted with accounting rules on consolidations whereby inter-company or segment profits are required to be eliminated, but *'transfer pricing within integrated operations [is] regarded as distorted if there is inconsistency in accounting treatment of agricultural produce before and after entry into trading or processing activities'* (para. 99).

### **2.3.6 Agricultural Land**

The SC regarded Agricultural Land as within the general scope of all agricultural activities. Land was often the single most valuable agricultural asset especially for small farming entities or family-owned enterprises which, worldwide, were the predominant form of farming organisations. Moreover, certain biological asset classes were not severable from the land, *e.g.* horticultural bearer assets. These assets were integrated and inseparable with a symbiotic relationship between land and its fertility, *terroir* and climate (paras. 101-6).

### **2.3.7 Recognition of Physical Changes in Biological Assets**

In common with DP 23, the recognition criteria (paras. 58-72) were that fair value changes should be allocated between physical changes, to be recognised in the income statement as income or expenses, and changes in the carrying values, attributable to changes in fair values, which should be recognised in reserves in the SONOME under the heading of surplus/deficit on fair valuation of biological assets.

The SC acknowledged there were other alternatives, *e.g.* all changes recognised through the income statement; separate identification of physical and value changes recognised in either the income statement or in reserves; or, recognition of both changes credited directly into reserves within equity, pending realisation.

Whilst the SC was unanimous the components should be separately identified, unanimity of treatment was not achieved. Therefore this was a critical item in the request for comment from submissions – refer Q. 9-12 in Appendix 10.

### **2.3.8 Presentation**

The DSOP contained extensive prescriptive commentary about how biological assets and produce should be presented in the income statement, on the face of the balance sheet and/or in notes to the financial statements (Principles 11-16 and 20, paras. 73-100). Most of these were the same as in DP 23.

The SC also envisaged a separate SGARA-asset class classified as neither current- nor non-current assets within the balance sheet. This would contain sub-classifications for each type of animal or plant, its economic functionality, *i.e.* whether ‘consumable’ or ‘bearer’, and their respective state of maturity or immaturity.

Further detailed disclosures were proposed relating to agricultural activities; bases for determining fair values; valuations; changes attributable to physical transformation and carrying values; title restrictions; risk management strategies and whether agricultural activities were sustainable and/or the date for cessation of such activities (Principle 16).

Likewise, agricultural produce should be separately classified within Inventories or disaggregated in the notes (Principle 20).

### **2.3.9 Guidance on Application of the Agriculture Standard**

Finally, the DSOP Appendix contained Illustrative Examples of accounting, work sheet reconciliations and model disclosures under DSOP presentation principles for dairy farming and forestry entities respectively.

### **2.3.10 Board Approval**

The IASC Board considered ‘A note from staff’ as Agenda Paper 15 , and not the SC, supporting issue of the DSOP at its Barcelona Board Meeting. [Appendix 10](#) contains the approved DSOP Principles and Invitation to Comment. The Board paper highlighted key issues and detailed all principal recommendations. The DSOP was approved for publication in November (IASB, 1996b).

## 2.4 Publicity Following Issue of the IASC's Draft Statement of Principles

### 2.4.1 Steering Committee Project Manager

One of the IASC's *Point Outline* process requirements was that the Project Manager advocates the DSOP proposals publicly. Apart from the IASC's own summary, referred to earlier, Kirton (1997) published an article in *Accountancy*. The abstract quotes:

The International Accounting Standards Committee (IASC), supported by the World Bank, is seeking to develop a standard applicable to all agricultural activities and entities, and its Steering Committee on **Agriculture** released a draft Statement of Principles at the end of 1996. Confronted with the diversity of agriculture, the Steering Group chose to do two things:

1. identify the characteristics of agriculture, which it defined as the management of the biological transformation of animals and plants to yield produce for consumption or processing.
2. consider the accounting implications flowing from these characteristics (p. 60).

The text summarised the principles behind the DSOP, the implications of the principal proposals, including fair value measurement and reporting treatment for changes in fair values, and the future stages envisaged towards promulgating the proposed new standard. This was expected to be issued in March 1999.

### 2.4.2 Other Publicity

Various journal articles announced release of the DSOP. These were published in professional magazines and summarised the main recommendations (*e.g.* CIMA, 1997, Feb.; IASC, 1997, Feb.; ASCPA, 1997, June; and ICANZ, 1997, May). One critical article from an ICAEW DSOP working party member was published from by B. Fone. He had sought views from U.K. agricultural specialists, practising firms, growers and agricultural agents. He submitted historical cost was the correct approach for profit measurement for short-term agricultural activities (ICAEW, 1997, June, p. 66):

the DSOP proposal was not the right approach for introducing earlier recognition of profit, before it was realised through sale of the product...with maturity [in the UK] of seasonal crops and horticulture following an annual cycle, and established accounting practice based on the historical cost concept is acceptable to the banks, and the revenue authorities.

Instead, the DSOP valuation proposals were deemed more applicable and appropriate for assets maturing after a long period, like woodland forestry, where it was possible to use NPV related to potential future yield.

## **2.5 Summary of Responses Received on the DSOP - Agriculture**

There is no information in IASC publications on the criteria for determining invitees to comment upon the DSOP and their %-response rate. However what is striking was the preponderance of submissions from fellow standard-setter bodies, regulatory agencies and IASC member bodies; as well as the major accounting firms.

Appendix 10 records the 16 questions for comment with requests for advice on any other matters germane to the project. Appendix 11 identifies the 42 Respondents. Submissions totalled over 450 pages with submissions ranging from an equivalent simple “I agree” to one of nearly 200 pages from the American Farm Financial Standards Council proposing guidance for accounting for agriculture on completely different principles and procedures.

In a study on political processes and lobbying the form of lobbying is instructive. Respondents were invited to submit and address comments to ‘The Secretary-General’. Twenty-seven did so including two addressed simply to the IASC. Fifteen personalised their submission to ‘Sir Bryan’ or ‘Sir Bryan Carsberg’, whether through familiarity or to seek greater attention to their response. Two went further by directly copying ‘W. McGregor’ as AARF Executive Director and technical adviser to the IASC Board. Another was copied to the ‘Canadian members on the IASC Board’, whilst the fourth, the AARF submission, was copied to Reyaz Milhular, SC Chairman – probably recognising his role as a key influencer in committee deliberations.

Table 15, below, summarises the total 42 respondents into groupings of principal standard setters, professional and other responders across general geographical areas. More than 60% of respondents were from the U.K./Europe and Australia/New Zealand. Three academics responded, but just four preparers and three users worldwide.



**Table 15. IASC DSOP Respondents by Geographical Areas**

Respondents	Pan-National	U.K./ Europe	Australia/ N.Z.	U.S.A./ Canada	South America	Africa	Asia	Total
Standard-Setting Bodies	1	1	1					3
Regulators/Auditors Gen.		1	1					2
Member Accting Bodies		6	3	3	1	2	1	16
Accting Firms/Practitioners	3	1	1					5
Public Sector	1			1				2
General Industry Group			1					1
SGARA Rep. Body		1						1
SGARA Forestry Coys			1			1		2
SGARA Consumable Coys		1	1					2
Non-SGARA Coy			1					1
Banks & Fin Institutions	1	2						3
Academics		1	2					3
Financial Analyst Group				1				1
<b>Total</b>	<b>6</b>	<b>14</b>	<b>12</b>	<b>5</b>	<b>1</b>	<b>3</b>	<b>1</b>	<b>42</b>

Source: Summary of Respondents in [Appendix 11](#).

Camfferman and Zeff (2007) noted that *'in October 1997 when the Board discussed responses to (the) DSOP issued earlier that year...it might have noticed that hardly any reactions had been received from developing countries'*. There were only three submissions from what might be regarded as the World Bank's developing and newly-industrialised country clients; that is, from Argentina, Malaysia and Zimbabwe. Furthermore, Camfferman and Zeff commented that the SC was concentrating its attention on conceptual problems with responders concerned that the DSOP was *'likely to set precedents and to have influence beyond the subject area, (also) several (IASC insider) board delegations began to express reservations about the proposed approach, both because of the wider implications as well as concerns over the reliability of fair value measurements for biological assets'* (p. 403).

One academic respondent, Colin Saunderson, from Cambridge University, and colleague of Professor Geoff Whittington technical adviser to the IASB, criticised the DSOP as *'well intentioned but too academic (it) will be totally incomprehensible to many in developing countries...(it) should be totally rewritten and accompanied by a "child's guide". The draft is unfortunately far too academic. Sorry'*.<sup>49</sup>

<sup>49</sup> Respondent 41 in [Appendix 11](#)

There was no reference then, nor concern expressed, that only four agricultural entities had responded. Two were forestry companies, from Australia and South Africa, one for livestock from New Zealand, and there was a U.K. conglomerate with pig and poultry breeding activities and salmon farming interests along with other ancillary activities servicing the agricultural industry. Each expressed critical and severe misgivings about the DSOP proposals.

However there was widespread acceptance amongst the 42 respondents for the need to bring accounting for agriculture into the main body of standards by removing exclusions in existing standards. There was less unanimity about the approaches being developed.

An underlying theme was that some respondents felt the wrong issues were being addressed, absent other work by the IASC. The proposal for 'fair value' measurement for agriculture over the conventional 'historic cost' basis was premature without prior conceptual framework consideration for value measurement concepts. Likewise, prior development work was recommended on the concept of income, role of the income statement in measuring period performance or for some wider performance-related comprehensive income statement.

Others favoured fair value, but with a sub-set hierarchy of measurement bases established when fair values were unreliable or irrelevant.

Respondents expressed apprehension about the stated use of fair value income accrual accounting as a proxy for biological transformation/asset growth where there was no contractual counter-party. They saw potential risk of unrealised holding-value gains/losses being recognised within the income statement which in turn might create fiscal liabilities. Furthermore, this also created enhanced expectations about actual cash flow generation, including ability to distribute dividends from those unrealised profits.

There were also concerns expressed by respondents about conflicts with existing standards. These related to proposals affecting *Financial Instruments* involving forward-pricing contracts for agricultural produce;<sup>50</sup> for leasing arrangements for agricultural assets; accounting for agricultural land, and the non-elimination of profits on consolidation between subsidiaries within an integrated agricultural parent entity.

Some respondents qualified their questionnaire responses, stating different recognition considerations exist for bearer- and consumable-SGARAs. DP 23 and the DSOP maintained agriculture was a uniform industry. These respondents disagreed.

The DSOP philosophy was that 'efficient and active markets' could be relied upon for fair value discovery for reporting purposes. However, respondents indicated this was not invariably the case due to unreliable or irrelevant pricing bases, short term supply or demand constraints temporarily impacting spot prices, Government price interventions or other market imperfections. This was particularly so for long term biological assets where a fair-value surrogate or modified-historic cost was considered a superior measure.

Further refinements were necessary as a result of the DSOP submission process. Early indication of changing AARF thinking occurred in AARF's DSOP submission dated 8 May 1997. The AARF appeared to use their submission as a public lobbying device to IASC Board members and to SC members that their views had changed.

The AARF supplied reasons why its proposed ED 83 Exposure Draft, to be issued three months later, would recommend changes in carrying value from biological transformation would be treated as a combined entry credited/debited in the income statement. Specific or general price effects should not be split between quantity and value components for reporting respectively in the income statement and reserves as the DSOP proposed.

Thus the AARF took this opportunity to lobby the IASC publicly and directly to 'correct' the DSOP's rationale especially where applicable to long-term forestry SGARAs.

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<sup>50</sup> N.B. IAS 39 *Financial Instruments* was still being developed at that time under Paul Pacter's responsibility. His key role in the establishment of the *Agriculture* standard is developed in the next chapter.

## 2.6 Australian Champions at the IASC

During the AARF's consideration of the DP 23 report and submissions, staff had already expressed their desire to panellists not to move ahead of other jurisdictions. However the AARF's ED 83 proposal 18 months later contained very different concepts to those in the IASC's published *Draft Statement of Principles* report (IASC, 1996b).

The question is whether changes made by staff to DP 23 were the results of internal lobbying and further internal consideration of the principles involved within the AARF, or the result of co-operation on these issues alongside consideration by the IASC's SC parallel DSOP development in London during the two year period following release of DP 23. Given the dates involved, and AARF's subsequent submission on the IASC's DSOP, the former was most likely to be the case. It appeared the AARF had decided to lobby to pre-empt IASC work and thereby influence the IASC's exposure draft preparation.

Camfferman and Zeff refer to the '*Australian champions*' (2007, p. 403). During the development of the IASC's Agriculture project these key individuals included:

***Table 16. Australian Delegates to the IASC During the Agriculture Project***

<b>Name</b>	<b>Period</b>	<b>Organisation</b>
Warren McGregor	1986-99	AARF Staff Observer/IASC Technical Adviser
Michael Sharpe	1990-97	Coopers & Lybrand & ICAA President
Geoffrey Heeley	1995-97	BHP Director
Jan McCahey	1995-98	AARF Staff/IASC Technical Adviser
Ian Hammond	1995-2000	Price Waterhouse & AASB Member
Kevin Stevenson	1996-99	On IASC Interpretations + Leasing Committees
David Boymal	1998-99	Arthur Young & AASB Member
Kenneth Spencer	1998-2000	Peat Marwick & AASB Chairman
Angus Thomson	1999-2000	AARF Staff/IASC Technical Adviser
Brian Morris	2000	Edwards Marshall & Co.

Source: Camfferman and Zeff (2007).

Any of these Australian delegates could have played significant promoter and/or 'key player' advisory, support and decision-making roles, as gatekeepers, influencing development of the IASC's *Agriculture* project, and as it progressed. Robert Keys was not included in the above list but was noted as an Observer on the IASC SC during 2000, and possibly earlier.

## 2.7 Summary

Each of the Australian and IASC standards setters had completed the first formal consideration stage towards developing respective *SGARA/Agriculture* standards.

Some key gatekeepers were already identified. Warren McGregor was a formal link between both the AARF and the IASC. There were other ‘*Australian champions*’ recognised by external observers. Robert Keys, Jan McCahey and Angus Thomson were key AARF technical staff members. However the UNE contractor, *i.e.* Don Roberts and other UNE staff, together with the project advisory panel, appeared only to have had an arms-length peripheral role not involved as internal AARF decision-making participants.

In the IASC there appeared to be split gatekeeper roles between staff reporting to the Board and the SC Project Manager reporting through the staff Technical Director, but sometimes direct to the Board. Each support group appeared to have separate responsibilities. The SC was seen more as a ‘working group’ staffed from constituent countries to provide worldwide experience and apparent involvement, whereas real influencing power lay elsewhere within the IASC. In addition, there were other Technical Advisers supporting some Board delegations, as summarised in Appendix 8A.

As foreshadowed already, the *inside access* institutional model predominated although external submissions were sought. Few preparers or users responded. At that juncture, it was too early to discern how responsive the gatekeepers would be to the wide variability between submissions. Few appeared to be lobbying *per se*; rather, highlighting problems or principles requiring further work and clarification. Even so, some were not wholly supportive – apart from confirming the need for an IFRS-standard for Agriculture.

Each of the Australian and IASC ‘Principles’ documents indicated technical accounting measurement issues were neither conformed nor complete – except each did agree that unrealised price effects in changes in asset carrying values should be credited to reserves. Apart from the AARF submission, no other DSOP respondent foreshadowed this eventual IASC exposure draft changes. This was the first evidence of inter-agency lobbying by the AARF ‘policy entrepreneurs’ who were completing their own internal initiative.

### Chapter 3. EXPOSURE DRAFTS

#### Introduction

Table 17 identifies key elements for this rule-making stage for the AASB and IASC.

***Table 17. Agenda Exposure Draft Process for Agriculture***

Stage of Rule Making	Elements	Modes of Lobbying	Evidence
<b>Formal Consideration of Agenda Items</b>	AASB issues ED 83. IASC issues E65. IASC also undertakes Field Test Project	Written submissions informal discussion	Written submissions, Journal & other media articles.

Source: Table 9 - summarising the *SGARA/Agriculture* standards processes.

The AASB issued its ED 83 *SGARA* Exposure Draft in August 1997; eight months after the IASC issued its Draft Statement of Principles (DSOP). The AASB received 46 submissions on ED 83. It was on a significantly different basis to DP 23 and the DSOP.

The IASC issued E65 *Agriculture* in December 1999 indicating it would also conduct a field test with preparers. It received 60 submissions on E65. Only six preparers responded. Numerous submissions asked for field test investigations and results. The IASC Board requested the SC undertake an urgent 'Field Test Project' (FTP) to gauge preparers' acceptance of the proposed GPFR 'fair value' concepts. This report has not been released publicly but its findings are included in full as [Appendix 15](#).

The analysis provides introductory comments on each exposure draft, submissions made by respondents, staff commentaries recorded in IASC publications and in the AARF staff's 'Basis for Conclusions'. Articles were also published by staff and external commentators. No public hearings were recorded, nor were minutes of Board meetings published.

The discussion compares the changes between respective 'principles' documents and exposure drafts. It highlights salient issues raised by respondents and identifies those rejected in progressing to final issue of the AASB 1037 *SGARA* standard in Australia in August 1998, and by the IASC for its IAS 41 *Agriculture* standard in December 2000.

### 3.1 Australia – Exposure Draft ED 83 Political Processes

ED 83 was issued in August 1997 (AARF, 1997).<sup>51</sup>

Previously, in October 1995, AARF staff had commented to advisory group panellists that Australia should not *'lead the world in promulgating standards'*. However ED 83 respondents claimed that was exactly what the AASB had done. The issue date for the IASC's DSOP was December 1996, with comments requested by 30 April 1997. Ten Australasian ED 83 entities had already commented to the IASC up to 3-6 months earlier. Accordingly, many respondents<sup>52</sup> recommended the AARF/AASB defer to the IASC process and wait. By waiting, the AARF would be able to, and should, lobby the IASC direct to ensure development of a conformed international standard - particularly since standards harmonisation was the ultimate goal but each was using different terminology and had different accounting treatments. Furthermore respondents claimed that if the AASB issued its standard before the IASC, Australian preparers would be obliged to respond to two different standards over a very short period.

Instead, the AARF decided to proceed alone because of *'uncertain IASC timing'*, an unstated urgent need for local guidance on SGARA accounting and *'implementation experience will be of benefit to the IASC as it finalises its Agriculture project'*. Thus the AASB would look for *'opportunities to continue to provide input...in the interest of harmony'* between the two standards (AASB, 1998, p. 23).

In effect, and as hinted in early publicity, the AASB appeared to be following a pre-emptive strategy against the IASC by prior completion of their exposure draft rule-making process and through early issue of their SGARA standard. For local credibility, the Australian delegates then had to lobby the IASC to influence the final issue of IAS 41 against other equally determined IASC Board delegations. This became an issue at the closing stages of IASC Board deliberations preparatory to issue of IAS 41.

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<sup>51</sup> The Exposure Draft ED 83 was prepared by the PSASB of the AARF and by the AASB.

<sup>52</sup> These included PWC, KPMG, Arthur Andersen, Ernst & Young, Coopers & Lybrand, BHP Ltd., Futuris Ltd., BRL Hardy Ltd., Amcor Ltd., and the ICAA.

### **3.1.1 Rural Industries Research Development Corporation (RIRDC) Grant**

While Roberts *et al.* (1995) were undertaking work on their DP 23 SGARA Report, the AARF began independently to conduct parallel internal research.

In early 1992, the AAFR obtained a grant from the Australian Government's RIRDC for its AAR-1A project titled *Development of an accounting standard for self-generating and regenerating assets* within the RIRDC's 'Resilient Agricultural Systems' category for 'Industry Training and Development – Financial Management' (RIRDC, 1999, Sept.).

The project start date was recorded as 30 June 1992 under the responsibility of Robert Keys, AARF Project Director. This was the date the UNE Group were originally contracted to complete DP 23. The total RIRDC project cost was \$108,000 of which \$72,000 was co-funded by the RIRDC (RIRDC, 2001, Dec., Chart 3.24, p. 154).

The original RIRDC target completion date was 30 September 1995. This was unlikely to be achieved since DP 23 was not finally issued until May 1995. Although the RIRDC required progress reports none were recorded in RIRDC annual summaries. The RIRDC was later to note, without elaboration, that '*there were problems with the administration of the project and the outcomes were delayed considerably*' (RIRDC, 2001, Dec.).

The writer sought a copy of the RIRDC Report. It was not available from the RIRDC and no Library copies are recorded. Only the Abstract was provided in the AARF's 'AAR-1A Report' to the RIRDC (1999, Sept.). This was submitted sometime prior to release of the AARF's ED 83 exposure draft in August 1997. ED 83 itself may have been attached as the project output. [Appendix 12](#) contains the full Abstract because of its significance as evidence of the Cobb *et al.* (1976) *inside access* model and its importance in the development of the final agriculture standards.

The Abstract demonstrates how far AARF technical staff had altered their views compared to discussions held two years earlier with advisory group panellists and reasons given for those changes as the basis for AARF's submission on the IASC's DSOP.



The contents varied significantly from DP 23. The principal conclusions were:

- SGARAs should be measured at current value, in particular net market value (NMV);
- the entire change in NMV in a period should be recorded in the Income Statement;
- at harvest the non-living produce of a SGARA ceases to be ‘living’ so, by definition, is no longer a SGARA;
- the harvested produce should be measured at NMV; this becomes the deemed cost of produce under the *Inventory Standard* since ‘*it would be unreasonable to require SGARAs to be measured at net market value and then to require the non-living produce extracted therefrom to be measured at cost*’;
- SGARA should be classified in the Balance Sheet as either current- or non-current assets in accordance with GPFR concepts.

These five SGARA accounting rules were the basis of the Australian AASB 1037 standard. They were telegraphed in the AASB submission on the DSOP and were influential in developing the final IAS 41 standard which was to emerge two years later.

### **3.1.2 Comparisons between the DP 23 SGARA and ED 83 SGARA documents**

There were other changes from DP 23 too. These are summarised for each key element:

#### **3.1.2.A. Scope**

##### ***DP 23:***

- to determine high quality GPFR requirements for reporting SGARAs held by the entity; and not special purpose reporting, *e.g.* for management, DP 23 Section 1.2, (Roberts *et al.*, 1995, pp. 2-4);
- the scope was determined by the definition of SGARAs as non-human related living assets, primarily forestry and livestock (Section 1.3, p. 5).

##### ***ED 83:***

- the scope was defined to apply to SGARAs held for profit or to generate produce for sale, including rights held through leases, or similar types of property arrangements. This definition excluded human and biotechnology assets, and SGARAs not held for sale or for production; including, for example, horses held for racing and recreational, heritage and ornamental trees, and native forests (AARF, 1997, para. 1.1).

### **3.1.2.B. Measurement of SGARAs**

#### ***DP 23:***

- estimated current market value (CMV) was the best method of SGARA valuation. If this were not available; an alternative surrogate valuation may be net present value (NPV) of cashflows, or a derived valuation of grape vines, or a forest, by valuing the entire vineyard, or forest, and deducting the value of land and improvements (*ibid.*, 1995, Section 4.4.2, pp. 37-50);
- contemplated a productive capacity concept of capital for SGARA-related entities (Section 4.4.2, pp. 46-9).

#### ***ED 83:***

- SGARAs to be measured at net market value (NMV) at each reporting date thereby recognising current stages of biological growth, current prices and the future economic benefits embedded in the SGARA (*ibid.*, 1997, para. 4.2);
- without active or liquid markets, the best indicator of NMV should be used to measure the SGARA...these may be alternatives such as the most recent net market price (NMP) of similar assets, NMP of related assets, NPV of cashflows expected to be generated, or, if none of these were available and reliable, then historic or compounded cost (para. 4.3.2).

### **3.1.2.C. Carrying Value Changes in SGARAs**

#### ***DP 23:***

- increment/decrement in CMVs should be separated into those due to physical changes and those due to price changes (*ibid.*, 1995. DP 23, Section 5.4-5.5, pp. 71-2 & Appendix 6);
- physical growth/impairment should be recognised as incremental revenue/expense in the income statement whilst price changes representing capital maintenance adjustments should be recorded in reserves (Section 5.5, p. 72).

#### ***ED 83:***

- any change in carrying amounts for the current reporting period must be recognised as revenue or expense in the income statement (*ibid.*, 1997, para. 4.4).

**3.1.2.D. Balance Sheet Classifications*****DP 23:***

- SGARAs to be reported as a category separate from current- and non-current assets (*ibid.*, 1995, Section 3, 3.3, 3.4, pp. 20-5).

***ED-83:***

- SGARAs to be presented in the balance sheet in respective current- or non-current asset categories, as determined by management (*ibid.*, 1997, para. 5.1).

**3.1.2.E. Disclosures of Financial and Non-Financial Information*****DP 23:***

- to identify SGARA types, quantities and qualities; any externally-imposed restrictions, *e.g.* logging quotas; extent of insurance relating to natural hazards, and inclusion of geographic segment topography and climatic information (*ibid.*, 1995, Section 7, 7.2.1, 7.2.2, pp. 81-3);

***ED 83:***

- quantities, extent and type of any restrictions on use; method adopted for a surrogate valuation, including significant assumptions and information to assess value sensitivity to changes in underlying assumptions, and whether directors' or independent valuer's valuations were used (*ibid.*, 1997, para. 6.1).

The differences between the DP 23 discussions with advisory group panellists and the ED 83 were significant. They were internally-derived as confirmed in the RIRDC Abstract. A key promoter was Robert Keys who led publicity on ED 83. From respondents' submissions, other 'key players' appeared to include Angus Thomson, Warren McGregor, as the AARF Executive Director, and Ian Mackintosh, Director of the PSASB. Unfortunately there are no formal minutes available for AARF/AASB deliberations to determine who else was involved and whether there was full unanimity or any concerns expressed during approval processes by other AARF/AASB representatives.

### 3.1.3 Publicity after Exposure Draft ED 83 Issued

In October 1997, an article in *The Accountant* reported issue of ED 83. The AASB was identified as the ‘*first national accounting body to release a draft standard on living assets, such as fish, orchards, livestock, racehorses (sic) and crops*’. The article broadly explained the changed AASB approach compared to the IASC’s recently published DSOP. Included were quotations from Robert Keys, then Senior Project Director, Accounting for the AARF:

ED 83 is exempted from the board’s efforts to harmonise Australian and International accounting standards...even so the AASB and IASC will work together and the Australian board will consider the IASC’s progress before finalising its own standard (Anon., 1997, Oct.).

This was the only reference found to any ‘*exemption*’ granted for ED 83, without any further elaboration on its basis, under whose authority, and for what reason.

Keys contributed an article for the *Australian Accountant* in November 1997 which set out ‘*a new perspective on recording living assets*’. The abstract reads in part:

ED 83 defines self-generating and regenerating assets (SGARA) as non-human living assets. Therefore ED 83 includes within its scope forests, livestock, crops, fruit bearers, and the living assets of aquaculturalists and stud breeders. ED 83 proposes that a SGARA should be measured at its current value, and that net market value be adopted as the current value attribute for SGARAs. The non-living produce of a SGARA, such as fruit picked from a tree, wool shorn from a sheep, or a felled log, is not a SGARA and falls within the scope of (inventory standards) AAS 2 and AASB 1019 (Keys, 1997, Nov.).

The full text acknowledged the earlier DP 23 work and recommendations by Roberts *et al.* (1995) and that ‘*wide consultation had occurred with representatives of SGARA-related industries (including public and private sector foresters) and members of professional bodies (including in the accounting and valuer profession)*’ (Keys, 1997, Nov.).

The first presumably refers to the advisory group panellists, but there is no other cross-reference to any other informal consultations prior to issue of ED 83.

It was therefore not altogether surprising that, except for the forestry sector, many submissions were critical of much in ED 83.

### 3.1.4 Submissions on ED 83

Table 18 provides an overview of the 46 professional and industry group respondents across Australasia (AARF, 1998b). There was no evidence of confidential or private submissions but that cannot be excluded. The full respondent list is recorded in [Appendix 13](#). 59% of submissions were supplied from 27 SGARA entities across the full range of public and private sectors, and 24% comprised responses from the ‘big-six’ accounting firms and three other chartered accountant practitioners.

***Table 18. Australia/N.Z. - ED 83 Respondents***

<b>Respondent Groups</b>	<b>Total</b>
<b>State Auditors-General &amp; Treasury Departments</b>	<b>5</b>
<b>Member Accounting Bodies/ Accounting Firms/Practitioners</b>	<b>11</b>
<b>SGARA Representative Bodies</b>	<b>2</b>
<b>SGARA Public &amp; Private Sector Forestry Companies</b>	<b>10</b>
<b>SGARA Bearer - Wine Companies</b>	<b>5</b>
<b>SGARA Consumable - Crop &amp; Livestock Companies</b>	<b>5</b>
<b>Non-SGARA Company</b>	<b>1</b>
<b>Academics</b>	<b>4</b>
<b>Valuers &amp; Financial Analyst Groups</b>	<b>3</b>
<b>Total</b>	<b>46</b>

Source: Summary derived from [Appendix 13](#), p. 58.

The political lobbying characteristics warrant comment. 31 were addressed, as requested, formally to the AARF ‘Executive Director’. However, nine respondents addressed their submissions to ‘Warren McGregor’ personally, whether because known personally or possibly to seek lobbying leverage at board level. Another was addressed, correctly in responsibility terms, to ‘Ian Mackintosh’, then Director of the PSASB, with oversight responsibility for the Tasmania Department of Treasury & Finance respondent.

More interesting however were the five submissions addressed directly to AARF staff members: four to Robert Keys – three from SGARA entities and one from a valuer - and one to Angus Thomson from the NSW Treasury. Thomson worked with Keys on the SGARA project and subsequently was seconded to assist on technical work for the IASC ‘with direct experience of research for standard setting’ (Camfferman and Zeff, 2007, p. 235). These five respondents probably recognised the key staff gatekeeper role, with scope to influence outcomes internally within the rule-making process.

There was one letter to W. McGregor from D.L. Roberts at UNE, not counted as a submission. It complained about lack of courtesy in not consulting or providing advance warning to him, or his two colleagues, prior to ED 83 publication about significant changes to DP 23. As noted earlier, they were contracted to undertake the SGARA development work for the AARF. Roberts then made two lengthy submissions recommending changes.

There were many technical and practical critical themes in the 46 submissions. These were discussed during Board meetings in February, March, May and June, including:

- ED 83 introduced new measurement concepts without agreed definitions and measurement criteria under the conceptual framework; it did not supply valuation methodology guidance. Nor was the role and primacy of the income statement addressed - whether for performance measurement, to reflect comprehensive income, or to differentiate between realised and unrealised components;
- questions were raised on consistency with the definition of an asset in the recently amended SAC 4 (AARF, 1995) whereby *'future growth projections in estimating NPVs [are] inconsistent with the definition of assets as future growth is not a past event and cannot be controlled by the reporting entity at the current reporting date'* (ACAG, 1998);
- concerns were expressed about unrealised profits being recorded in the income statement from harvested SGARAs being valued at NMV years before actual realisation and without any transfer of risk or ownership;
- concerns were expressed about recording changes in carrying values at each reporting date, potentially creating shareholders' expectations about availability of distributable profits, and potential reporting problems through identifying current taxation liabilities;
- whilst the measurement bases and current value hierarchy were clear, in practice 'active and liquid markets' for immature SGARAs just did not exist. Transparent price discovery and reported values would not be reliable. There was the risk they would be unduly subjective, or open to manipulation. In any case, inter-entity comparability was lost because of differing valuation assumptions;
- bearer-SGARAs were not severable from the land; and, if severed the SGARA asset was no longer saleable as an asset or realisable at a derived NMV-by-deduction valuation method;

- concerns were expressed that price change and biological growth were not the sole determinants of SGARA value; for instance, *terroir* quality has perceptible value, and value may occur elsewhere within an integrated entity, *e.g.* in winemaking or marketing skill. Each had a material shared-impact on the source value not attributable solely to deemed NMV of the SGARA asset itself. This was separate from concerns about unrelated balance date spot price impacts on real value from short-term spot supply disruptions or demand constraints;
- whilst there may be difficulties in separating price and growth changes, *e.g.* for forestry, this has been accepted practice for decades for livestock without problems of comparability, reliability or consistency; therefore the proposed change for this particular SGARA category was not warranted;
- respondents recommended preparers be surveyed to determine whether NMV is always relevant and practical and that users' views be considered on the reliability of deeming NMV for an immature SGARA in unmarketable condition, *i.e.* as proposed for interim reporting;
- consolidation of SGARA and non SGARA subsidiaries in integrated entities meant unrealised intra-group profits on inter-subsidiary trading would not be eliminated on transfer so that revenues may be double- or triple-accounted over time; and
- criticism that the proposed opening balance sheet transitional provisions will lock-in the recorded difference between NMV and cost into reserves within equity, so that on realisation this 'profit' was unable to be transferred to the income statement and therefore 'lost' for future dividend distributions under the Corporations Law.

Some respondents traversed the logic of the proposal. Since the AARF claimed use of current values was superior, more relevant and reliable than historic cost, then for consistency, these merits should be considered and applied to benefit all other standards. Moreover, if NMV valuation for SGARAs at harvest became the deemed cost for inventory, then NMV should become the preferred inventory valuation basis for all other own-produced, non-SGARA products. Accordingly, they recommended reconsideration of the conceptual basis for inventory accounting occur rather than allow a piecemeal and inconsistent development to apply solely for agriculture under the *SGARA* standard.

Some questioned whether an omnibus standard for all types of agricultural activity was the best way to establish a workable standard for agriculture. There was no logic behind having the same valuation rules for forestry, crops, aquaculture, livestock and orchards. Instead, there should be valuation rules for sectors applicable to their biological type not simply because they were ‘living’ or ‘non-living’ assets, *e.g.*:

- immature bearer- and consumable-SGARA – to value at historic cost or modified-HC;
- mature consumable-SGARA – to value as for inventory, at lower of HC or NMV;
- bearer-SGARA providing ongoing produce – replacement cost may be a superior indicator of fair value even although these SGARAs are integrated with and non-severable from the land (ACAG, 1998; EY, 1998).

It was evident some considered agriculture was not sufficiently different from other industries to warrant separate accounting treatment and valuation bases; instead better definition of measurement and reporting rules was required. In practice, SGARA entities had evolved virtually common measurement and GPF reporting rules worldwide – except for forestry. The standard was being devised principally for forestry. A separate standard was required rather than extrapolation of forestry’s special features to all SGARAs.

### **3.1.5 The Boards’ Response to Some Submissions**

The AASB and PSASB Boards, with AARF staff, countered five of these objections in their ‘Basis for Conclusions’ as an attachment to AASB 1037 issued a year later, in August 1998 (AASB, 1998).

The Boards’ discussion referred to submissions which recommended the standard should not apply for:

- SGARA with short term production cycles where historic cost (HC) principles were more appropriate;  
the Boards maintained financial performance occurs as biological change occurs rather than when the produce is sold. However, the Boards conceded that HC for short-term SGARAs may be the best indicator of NMV at a reporting date;
- bearer-SGARAs like grape vines and land were claimed analogous to other property, plant and equipment so should be accounted similarly;  
the Boards maintained the fundamental ‘living’ characteristic was the defining characteristic of the standard and that HC does not adequately embody ‘*future economic benefits and the financial performance of such SGARA*’. This comment ignored the fact



that such industries had accounted on a modified-HC basis with frequent directors' or external valuations for SGARAs and non-SGARAs alike;

- the impossibility of segregating SGARAs, *e.g.* vines, co-existing with its non-SGARA integrated land asset;

the Boards did not accept this since *'the "living" characteristic provides an appropriate basis for the defining scope of the standard and therefore the non-SGARA should be excluded'*. Thus the NMV within the integrated asset value should be disaggregated to determine the carrying value for each of the SGARA and the land, the latter accounted under its applicable PP&E standard;

- absence of liquid and active markets;

the Boards maintained professional valuers would use professional judgment to determine value. Appropriate full disclosures should occur to help assess the reliability of the reported carrying amounts.

This comment ignored the costs involved and impracticality of conducting frequent external valuations at every reporting date, in particular for Interim Reports;

- change from DP 23 whereby differences in SGARA carrying values were split between growth, for crediting to the income statement, and price effects to reserves as a capital maintenance adjustment in equity consistent with other standards;
  - the Boards doubted it was *'practical to separate change in value into its price and biological components without making an arbitrary allocation'* and countered that the proposed treatment is consistent with recent insurance and superannuation precedents for AAS 25 (1993) and AASB 1023 (1996);<sup>53</sup>
  - the Boards added that including combined price and quantity value changes in the income statement *'provides more relevant information to users of financial reports on a more timely basis than recognising changes as capital maintenance adjustments included directly in equity'*. This occurs much sooner for long-term SGARAs, like forestry, than with cash realisation many years later;
  - the Boards also maintained it was *'open to management (sic) to choose to appropriate an amount to profits to a reserve to indicate to shareholders the potentially un-distributable nature of the profits'* (AASB, 1998, p. 24).

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<sup>53</sup> AAS 25 *Financial Reporting by Superannuation Plans, 1993 revised*; and AASB 1023 *Financial Reporting of General Insurance Activities, 1996* were considered by the AASB as a precedent. Respondents claimed this was an irrelevant, incompatible monetary precedent not applicable for tangible SGARA assets.

### 3.1.6 Summary

Preparation of the final *SGARA* standard was virtually complete. In calling for submissions the Boards had stated they would '*prefer that respondents express a clear overall opinion on whether the Exposure Draft, in general, is supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on the major issues in the Exposure Draft*' (AARF, 1997, Preface, p. 5).

Already there were numerous principled and practical critical comments. Some were addressed in the Boards' *Basis of Conclusions* to the Standard; but others were not. Given the objections, critical comments and constructive recommendations to amend ED 83 proposals from experienced respondents, there was no policy learning evident by key insiders (Sabatier and Jenkins-Smith, 1993). There were no material changes in the eventual AASB 1037 *SGARA* standard.

However, once ED 83 was issued in August 1997, the AARF/AASB created an exposure draft precedent for the IASC. There was benefit in each agency being able to consider local Australian responses for developing respective standards internally. This was the inter-agency context for the IASC to move to its next rule-making stage, *i.e.* preparation of the *Agriculture E65* exposure draft.

E65 was issued nearly two years later, in July 1999, but not before considerable change to its previous DSOP proposals, partly because of changes in key personnel and partly from internal politicking within the IASC.

### **3.2 IASC – Exposure Draft E65 Political Processes**

The information supporting this discussion is derived from the IASC's periodic 'Insight' newsletters and Annual Review Reports together with commentary contributed by staff in the 'Basis for Conclusions' in Appendix B to Exposure Draft, E65 (IASB, 1999).

The IASC embarked on its exposure draft deliberations after receipt of all DSOP submissions during the first quarter, 1997, through to issue of E65 *Agriculture* Exposure Draft at the June 1999 Board Meeting (IASB, 1999). Meanwhile the AASB had pressed on with issuing its AASB 1037 *SGARA* standard in April 1998 placing additional political pressure on the IASC over the next fifteen months. There were marked technical changes from the DSOP. These reflected the influence of the AASB's ED 83 and AASB 1037. There were also important key personnel changes within the IASC. The end result was the IASC Board obtained the barest minimum two-thirds vote to approve issue of E65.

The IASC recorded receipt of 62 submissions on E65.<sup>54</sup> The Board noted very few responses from preparers, or from under-developed countries. Therefore it requested the SC undertake a Field Test Project (FTP) during the second quarter, 2000, to determine the acceptability of the 'fair value' proposals for measurement of and accounting for biological assets in Exposure Draft E65. There were 20 recorded FTP submissions. This project has not been reported before. Appendix 15 contains the results and comments supplied to the Board as Agenda Paper 7G for the Copenhagen Meeting.

The Board papers and official record of submissions for E65 (in Appendix 14) and for the FTP (in Table 21, p.166) contained two fewer submissions than reported above in Appendix B of the final IAS 41 standard. One possibility is that two confidential submissions on each were not recorded officially; alternatively, that a report from the Board's technical advisers and/or the SC accompanied the usual staff '*wrap-around introductory text*' (Camfferman and Zeff, 2007, p. 377) and were counted as two further submissions, presumably in support of the proposal to progress with the new standard.

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<sup>54</sup> The number of respondents on E65 and the Field Test Project was quoted from Para. B2 in the Appendix B Staff Commentary to the final IAS 41 *Agriculture* standard.

### 3.2.1 IASC Key Staff Insiders and the Steering Committee

Dr Liesel Knorr was the IASC's Technical Director after the DSOP was issued. She provided a review of responses received on the DSOP to the Board (IASC, 1997, June). She subsequently reported on directions given by the Board for developing work programmes arising from the DSOP responses and for considering exposure draft preparatory work. Knorr also acted as a staff conduit to Kirton, as SC Project Manager, who had similar working responsibilities (IASC, 1997, Dec.).

Paul Pacter was appointed as Project Manager to replace Ian Kirton during 1998. Pacter started his career in 1968 at New York University, before transferring to a medium-sized firm which merged into KPMG. He then worked with the Accounting Principles Board (APB) and later the Financial Accounting Standards Board (FASB). From 1984-89 he was appointed vice-chairman of the advisory council to the US Accounting Standards Board. In 1996 Pacter was appointed an IASC 'International Accounting Fellow' staff member.

Pacter was a key and influential promoter involved with internal IASC technical and political processes. He was a leading proponent for international standards harmonisation. Pacter's profile and experience also enabled him to proselytise the new IASC standards; for example and amongst others, he was responsible for and championed work on the IAS 39 *Financial Instruments* standard.

### 3.2.2 Switch to 'Fair Value'

In August 1998, Pacter made a major presentation to the 1998 American Accounting Association Conference in New Orleans entitled *International Accounting Standards Committee Update*.<sup>55</sup> In a three hour wide-ranging presentation and discussion across IASC history, current developments and future plans, he showed a slide on *Agriculture*. This referred to the AASB's ED 83 position that 'harvest' was the critical terminal event for agricultural produce. In the recorded discussion, Pacter confirmed his IAS 39 fair value mark-to-market credentials and by stating that 'fair value' balance sheet carrying values

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<sup>55</sup> <http://aaahq.org/AM1998/cpe/98cpe37.htm>.

The full transcript is at <<http://www.trinity.edu/rjensen/acct5341/speakers/pacter.htm>>

were equally applicable for agriculture. His presentation slide (No.33) illustrated the tentative SC position that Biological Assets unique to Agriculture should be valued at Fair Value....with Market Value being the starting point to determine Fair Value.<sup>56</sup>

Although Pacter had been involved with the project during 1998, on completion of the IAS 39 *Financial Instruments* project during the fourth quarter, 1998, the *Agriculture* project became his next major responsibility. This involved finalisation and issue of Exposure Draft E65 prior to his retirement from the IASC in June 2000.

### **3.2.3 Post-DSOP Review Work**

During the first half-1998 the IASC considered responses to ED 83. Knorr noted differences between the IASC's DSOP and AASB's ED 83. The principal one was elimination of the SGARA carrying value allocation between price and biological change. There were also other changes to be considered because of DSOP submissions. These included:

- existence of a market value was not necessary for the application a fair value;
- although fair value measurement was the relevant measurement basis for biological assets, with current market value providing a useful indicator, it was not necessarily the sole determinant;
- doubts were expressed over the practicality of separating value from physical change. More work was required to determine whether both components should be reported in the Income Statement especially as financial analysts had advised separate components were very helpful analytically;
- lack of support for the proposal that post-harvest produce should be valued at fair value for inventory. At Board instigation the steering committee was requested to undertake a special study on produce with long maturation periods;
- agricultural land to be excluded from further consideration but *'the Board directed the steering committee...consider the need to require fair value of agricultural land in specific circumstances'* (IASC, 1997, Dec.).

The Board had not given full support to the proposals outlined above even though these views appeared to have staff support. While staff were considering some of these matters, the SC was completing work to release a draft ED to the Board in July 1998, also having considered the DSOP and ED 83 comments.

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<sup>56</sup> *N.B.* This was in apparent contrast to the AARF/AASB position that, unlike for a non-monetary asset, a SGARA's NMV represented Market Value netted-back to the 'farm-gate'.

### 3.2.4 Inventory with Long Maturation Periods

The outcome from extending the project scope to include wine and similar products with long maturation periods was reported in the March 1998 'Insight Supplement'. Some of these products related to integrated enterprises, whilst in some jurisdictions they were officially designated as agricultural produce. However the SC returned to the theme that historic cost methods do not '*consistently provide the most relevant and reliable measurement of expected future benefit of this class of assets*' (IASB, 1998a, March, p. 15). The SC prepared a table on agricultural maturation examples:

**Table 19. IASC - Nature of Agricultural Products and Maturation Processes**

<b>Agricultural Produce</b>	<b>Process</b>	<b>Maturation</b>	<b>Product</b>
Grape	Fermentation Distillation	1-20 years 3-20 years	Wine Brandy
Milk	Curdling	1 year 2-3 years 5-7 years	Edam Parmesan Saanen
Sugar Cane	Distillation	2-20 years	Rum
Barley, Corn, Wheat	Distillation	2-30 years	Whisky
Pork	Curing	1-2 years	Prosciutto di Parma
Apples	Distillation Fermentation	1-15 years 5-30 years	Calvados Cider

Source: IASC Insight Supplement, IASC 1998b, March.

The committee's conclusions were that:

- harvest and processing for 'raw produce' was a comparatively short period compared to maturation aging processes;
- after initial stabilisation the end-product for maturation and marketing became an identifiably different product, *e.g.* grape juice *vs.* wine;
- timing of marketing was a maturation and consumer-related decision unrelated to the biological produce at harvest; moreover
- a winery, for example, does not necessarily have all own-sourced produce so it was not clear how purchased fruit could be brought within the scope of the project (IASB, 1998b, March).

Reference to third-party bought-in fruit was a *non-sequitur* for harvested non-living produce. By definition, these purchases were subject to the IAS 2 *Inventory* standard. That aside, the SC recommended the standard exclude maturation after harvest - even though there might be an economic rationale for integrated agricultural operations to control all activities, costs, quality and managerial expertise through the full supply chain from land to end-consumer.

### **3.2.5 Preliminary Work on the IASC Exposure Draft**

Although the proposed agriculture exposure draft was discussed at the Board's Washington Meeting in March 1999, approval was deferred until the Warsaw meeting held at end-June, 1999 (IASC, 1999, March). No reason was given for the delay. This may have resulted from apprehension E65 might not receive formal Board approval.

In the June 1999 Insight Newsletter, Pacter provided a lengthy outline of the proposed exposure draft titled *IASC Cultivates a New Standard on Agriculture* (IASC, 1999, June). The main features and rationale given were:

#### **3.2.5.A. Scope**

The draft ED would prescribe the accounting treatment for biological assets during the period of growth, procreation, and degeneration, as well as the initial measurement of agricultural produce at point of harvest. At that point, produce became 'inventory' to which the IAS 2 *Inventory* standard would apply. The proposal did not deal with further processing of agricultural produce after harvest which was regarded as 'manufacturing'.

#### **3.2.5.B. Measurement**

A key proposal was that all biological assets and all agricultural produce at the point of harvest be measured at each balance date at their market price 'fair value'. The Board believed that

- value changes provided better information about the performance of an enterprise's agricultural activity than the more traditional historical-cost-based measure of profit or loss; moreover
- reliable measures of 'fair values' of biological assets and agricultural produce at the point of harvest were presumed to be available and can always be determined. Since cost-based measures were often claimed to be of questionable reliability and usefulness in an agricultural context, measurement guidance would be provided, including that cost may be an appropriate indicator of 'fair value' in certain circumstances.

### **3.2.5.C. Reporting Changes in Values:**

While there appeared to be general Board consensus that biological assets should be measured at fair value, the Board had not yet concluded how changes in fair values of biological assets should be reported.

Pacter reported the Board was still considering the following alternatives:

- changes in fair values of biological assets should be recognised in the income statement as net profit or loss in the period in which the changes occur;
- changes in fair values of biological assets should be recognised directly in equity, through the statement of changes in equity, until the produce was **sold or consumed**, at which time the cumulative change in fair value previously recognised in equity should be included in net profit/loss for the period;
- changes in fair values of biological assets should be recognised directly in equity, through the statement of changes in equity until the agricultural produce is **harvested**, at which time the cumulative change in fair value previously recognised in equity should be included in the income statement as net profit or loss for the period;
- changes in fair values of biological assets should be recognised directly in equity, through the statement of changes in equity and never be reported in the income statement, *i.e.* not ‘cycled’ into revenue/expenses; and
- an enterprise should be given the choice between either immediate recognition in the income statement or recognition in equity pending sale or consumption, similar to the choice in IAS 39, *Financial Instruments: Recognition and Measurement*.

### **3.2.5.D. Agricultural Land**

There would be no special accounting rules for agricultural land. Instead it was proposed the accounting treatment for agricultural land would be identical for all other land under IAS 16, *Property, Plant and Equipment*.<sup>57</sup>

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<sup>57</sup> *N.B.* This created a *conundrum* for preparers, and users. Ordinary building and asset improvements attached to land were subject to IAS 16 *PP&E* standard accounting measurement and treatment; whilst buildings attached to land were treated differently under IAS 40 *Investment Properties*, and different again for biological assets attached to land under IAS 41 *Agriculture*.



### **3.2.5.E. Disclosures**

The exposure draft would require the carrying amount of each group of biological assets reported in the balance sheet to be separated and dis-aggregated in two ways:

- separate disclosures between consumable- and bearer-biological assets; and
- within each consumable- and bearer-classification, separate disclosure for mature and immature biological assets.

The Board believed that users of financial statements needed more detailed information about an entity's biological assets than a single total carrying amount. The ED would encourage an analysis of expenses on the face of the income statement, using a classification based on the *nature* of the expenses, *e.g.* fertiliser, wages and salaries, and depreciation. The alternative would be classification based on *function*, *i.e.* cost of sales, selling expenses and administration expenses. IAS 1 permitted both treatments.

### **3.2.5.F. Effective Date and Transition**

At transition date on initial adoption, it would be proposed that an adjustment to the previous carrying amount of biological assets, agricultural produce, and agricultural land should be recognised as an adjustment of retained earnings, rather than in net profit and loss as in AASB 1037. This latter item was amended during the Board meeting to conform to IAS 8, *Unusual and Prior Period Items and Changes in Accounting Policy*.

What was not clear from the article was whether Pacter was reporting an agreed Board view, that of some of the Technical Delegates, or solely from his role as Project Manager. Under the Cobb and Elder (1983) analysis, the role of institutional staff was that of key advisers, who undertook work for and informed the Board especially if it met only at infrequent intervals. More likely, the text probably reflected the status of his advice to the Board or the views of only a few key Board members and Technical Delegates.

The Board planned to discuss the Draft at its June meeting in Warsaw and approve it for publication afterwards (extracts from IASC, 1999, June). Pacter reported the Board had agreed to release Exposure Draft, E65, *Agriculture* in July 1999 (IASC, 1999). This was confirmed in the next Insight Newsletter sub-titled *IASC is ploughing new ground in a field not covered by an existing International Accounting Standard* (IASC, 1999, Oct.).

### 3.2.6 Issue of Exposure Draft E65 Agriculture

E65 (IASB, 1999) was issued with virtually identical principles to the AASB's ED 83. Some terminology was simplified, e.g. a SGARA became a biological asset probably reflecting submissions on ED 83. However there was one significant difference. ED 83 adopted *net market value* as the measurement basis whereas E65 referred to fair value. In contrast to ED 83, the E65 concept was a general market-place value, without deduction of transport or selling costs for net-back to the farm gate. This appeared to reflect Pacter's influence in transferring mark-to-market monetary precedents from IAS 39 to E65.

There was a final comment in Pacter's article that '*we are particularly interested in testing by companies based in emerging market countries, in addition to more developed countries*' (IASB, 1999, Oct.). The preamble to E65 also stated '*the Board intends to conduct a field test of the proposals in this exposure draft and invited participation*' (IASB, 1999, p. 3). There was no subsequent comment reported in any IASB publication about the Field Test outcome and how it influenced the final *Agriculture* standard.

Camfferman and Zeff expanded on the political processes at Board level and the reasons for the prolonged exposure draft process. Internal concerns were wider than the agriculture project. They reflected the concurrent deliberations on *Investment Property* as '*harbingers of a fundamental change in financial accounting*' in particular over the '*wider implications [of the proposed fair value approach]*' (2007, p. 403).<sup>58</sup>

Camfferman and Zeff recorded this was '*one of only two occasions in the IASB's history when an exposure draft was passed with just the required minimum of two-thirds of the votes*'. This was because there were '*no votes from the Swiss Industrial Holding Companies, Canada and the United States, with India and Germany abstaining*' (p. 403). Abstention was equivalent to a no-vote. For formal approval of the final standard the approval threshold increased from a minimum two-thirds to three-quarters approval by voting delegates (IASB, 1993, July). One delegate would have to change their vote on the merits of the proposed standard or because of a political compromise process.

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<sup>58</sup> This was issued as E64 in July 1999 and as IAS 40 *Investment Property* in March 2000.

The European and North American representatives used the opportunity to express their misgivings. The issues for dissenting delegations were '*whether it was appropriate to measure biological assets at fair value, whether such measurement would be reliable and whether the case against measurement at historical costs had properly been made*' (*ibid.*, 2007, p. 403). These issues were to continue up to the final vote on the new standard.

In addition, the abstention by the Indian/Sri Lankan delegation on the exposure draft vote might also indicate dissension within the SC. At the time there were six committee representatives: the chairman was from Sri Lanka, who was also an IASC voting delegate, and committee members were from France, New Zealand and Thailand; Pacter was the Project Manager and there were two observers from the World Bank and Zimbabwe. Depending on how representatives voted, any one of Mitnick's (1980) advocate or other archetype 'insiders' could have held a deciding vote within the committee to ensure progress of E65.

### **3.2.7 Publicity on Release of E65 Agriculture**

During internal deliberations prior to release of E65, media articles recorded progress on the concurrent proposed *Investment Property* and *Agriculture* standards, each adopting fair values. These appeared to be informed leaks. There was reference to Board disagreement especially from international delegates with the Board split 'roughly 50:50' about use of current values (Stokdyk, 1999, March), and the need for further conceptual work for reporting changes in carrying values in the income statement (Anon., 1999b, Aug.). Positive feedback was given in support of the project from Malaysian member authorities (Baharuddin, 1999, April; Anon., 1999b, April).

Negative comments were expressed too (Anon., 1999a, Aug.). This article reported the continuing spat on AASB 1037 between the AASB and the local G-100 Group.<sup>59</sup> The G-100 National President, Bryce Dennison, was also reported to have lobbied the IASC direct.

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<sup>59</sup> The G-100 group is an association of senior accounting and finance executives representing the major listed public and government-owned enterprises in Australia.

There were concerns expressed about both the inability to find a reliable enough method to determine NMVs for all agricultural assets, and issues with the transitional prohibition on recognition of unrecorded 'gains' through the income statement for dividend distribution purposes. The article reported the *IASC Board had decided the Australian standard could be the foundation of the IASC's own exposure draft.* The AASB Chairman, Kenneth Spencer, described this as *'a vindication of [AASB] efforts'* when responding to criticisms for issuing their standard *'ahead of the rest of the world'* (Anon., 1999a, Aug.). This was confirmed independently (Camfferman and Zeff, 2007, p. 403).

Apart from general reporting on the release of E65 (e.g. Anon., 1999b, Aug.; Anon., 1999b, Sept.) three further articles argued in favour of the proposed exposure draft. The first was from the IASC Secretary-General, Sir Bryan Carsberg. He also noted *'IASC plans to conduct a field test of the [E65] proposals'* (Anon., 1999a, Sept.).

The other two were by Paul Pacter, as Project Manager. The first was an explanatory article outlining the basis for conclusions about key proposals in E65. Pacter confirmed too *'the Board intends to conduct a field test'* and that *'the proposals...are substantially similar to those adopted in Australia'* (Pacter, 1999a, Sept.).

The second dealt with the conceptual options hindering progress on the concurrent *Investment Property* (E64) and *Agriculture* (E65) deliberations through reporting fair values in the balance sheet and changes in carrying value through the income statement. Pacter expected fair value principles would feature in other current and planned projects, such as accounting for the insurance industry, the extractive oil and gas industries and for other future projects (Pacter, 1999b, Sept.).

Pacter appeared to be indicating publicly that future fair value applications were being advocated and proselytised by key insiders without necessarily having achieved full consensus within the Board. These initiatives can be styled as pursuit by *'issue entrepreneurs'* to achieve their aims (Cobb and Elder, 1983, p. 187).

### 3.2.8 Comment Letters on E65 - Agriculture

Table 20 summarises the principal groupings of respondents in [Appendix 14](#) by general geographical areas.

**Table 20. IASC - E65 Respondents by Geographical Areas**

Respondents	U.K. / Europe	Australia/ N.Z.	U.S.A./ Canada	South America	Africa	Asia	Total
Standard-Setting Bodies	3	1		1		1	6
Regulators/Auditors Gen.	1	1					2
Member Accounting Bodies	10	2	3	1	4	4	24
Accounting Firms/Practitioners	3	2	1				6
General Industry Group	1	1					2
Agriculture Rep. Body	1		1				2
Ag. Forestry Companies		1					1
Ag. Consumable Crops	1	1			2		4
Ag. Bearer Companies		1					1
Non-Agricultural Crops	4						4
Academics	1	1				3	5
Financial Analyst Groups			2			1	3
<b>Total</b>	<b>25</b>	<b>11</b>	<b>7</b>	<b>2</b>	<b>6</b>	<b>9</b>	<b>60</b>

Source: [Appendix 14](#), p.60 - Reported IASC List of Respondents and Submissions.

60% of submissions were received from standard-setting, regulatory and member and other accounting bodies; few were supportive of E65 proposals. Only one of the major accounting firms was generally supportive; and, of the others, only if significant changes occurred. The six agricultural company submissions were critical of most aspects of E65; in particular, the impracticality of excluding some post-harvest processing for certain consumable crops and the operation of the proposed standard for bearer entities.

Fourteen submissions were from respondents with delegates who had voted against introduction of E65. Five may be considered 'collusive' being virtually identical in form and content. None of them had direct agricultural interests. Rather, each objected on principle that the 'fair value' concept and reporting methodology for a minor standard would create an important precedent for wider application for other non-financial assets.

Principal themes in submissions by respondent categories are summarised below.<sup>60</sup>

<sup>60</sup> N.B. Comments by Academics are discussed across all rule-making stages in [Section 5.4](#) below.

### 3.2.8.A. Comments from Agricultural Entity Preparers

Australian-listed **East African Coffee Plantations Limited** (EACP, 2000) was opposed, except for livestock where active markets existed. The principles were too broad. Investors could be misled by manipulated results, exaggerated by recording unrealised profits. In turn these could create unwarranted dividend expectations. EACP contended long-life assets should be held at cost. Changes in values should not be treated as deemed revenues based upon assumed future prices, costs, yields and market conditions.

South African-based **Illovo Sugar Limited** (Illovo, 2000), with operations in five southern-African countries, highlighted the unreality of valuing harvests spread over many months where assets with a 12-24 month growing cycle were divided between mature and immature root-balls and cane. In Illovo's operations fair value was not the best indicator. Valuation should be based on recoverable amounts determined in a prudent manner.

**Eastern Produce Kenya Ltd.** (EPK, 2000) was critical of the proposal for tea plantations. Methods for establishing cost were well understood and objective. EPK did not accept cost-based measures were of questionable value as claimed in E65. Tea plantation operations were completely different from what E65 described: tea bushes have a life of over 50 years, valuations on an NPV basis where operations are subject to weather and pricing vagaries lack reliability. Most importantly, a tea bush is harvested every ten days. Pre- and post-harvest valuation is completely unrealistic and inappropriate as a performance measure; lastly, there is no practical market for the harvested green tea-leaf without further processing. The latter activity was specifically excluded from E65.

Australian **North Group Limited** (North 2000) had made an earlier DSOP submission. It had also submitted on ED 83. North offered to assist in the Field Test. It claimed there was insufficient valuation guidance in AASB 1037. E65 was similarly defective. More importantly, E65 was incompatible with the IAS 40 *Investment Property* standard which allowed a cost or fair value option for a standard less complex than Agriculture. Thus North recommended reconsideration of 'fair value' for biological assets and whether all carrying value differences be proposed reported within the income statement. They also

recommended the G4+1 (1999) income and performance measurement project proposal be accorded higher priority before finalising the Agriculture standard.

Netherlands-based **Nutreco International** (Nutreco, 2000) strongly urged against issuing the proposed standard because:

- fair value cannot be measured reliably prior to a realisation event;
- changes in fair value being recorded in the income statement are not the most appropriate management performance indicator; and
- E65 is in conflict with the IASC Framework predicated on recoverable historic cost.

Australian-listed **Southcorp Holdings** (Southcorp, 2000) expressed serious concerns. It regarded the proposal as an academic approach universally condemned by wine and other Australian agricultural interests. Southcorp urged a Field Test occur to determine the proposal's practicality. It offered to assist. It argued that recording unrealised gains in the income statement had adverse consequences for dividend expectations. In addition, U.S.A. lenders were notoriously suspicious of enhanced income-earning treatments which made financial statements more opaque. Constructively, Southcorp urged that consideration be given to recording unrealised values in reserves, for later cycling on realisation to the income statement. Southcorp would only endorse the proposal after the IASC had completed and reported back on the Field Test, and after implementation of the G4+1 (1999) performance measurement project, including cycling.

### **3.2.8.B. Comments from Standards-Setter Bodies**

The **Australian Accounting Research Foundation** (AARF, 1999) endorsed the merits of its ED 83 SGARA accounting methodology. Apart from discussing treatment of leases for agricultural activities, their other comments clarified E65 anomalies and drafting issues. In particular, AARF emphasised that net market value was the most relevant and reliable measure at point of harvest, after deducting harvesting, pre-sale and transport costs so that inventory carrying value after harvest would not exceed expected net sale proceeds.

Qualified support was given by the **Danish Accounting Standards Committee** (DASC, 2000), but it identified issues on treatment of intangible agricultural assets, *e.g.* milk quotas, rights to raise potatoes and government grants on limiting the size of arable farms.

The **Instituto Mexicano de Contadores Publicos** (IMCP, 2000) standards setter also endorsed E65 but recommended further simplifications, including fewer disclosures.

The **Malaysian Accounting Standards Board** (MASB, 2000) gave only qualified support. It recommended not all agricultural activities be included in one standard. Whilst produce might be measurable at fair value in some cases, it was not a reliable basis for long term consumable- or bearer-entities. It recommended changes in carrying value be credited to reserves, pending realisation, because where these were included in full in the income statement there would be difficulties in managing dividend expectations. Some jurisdictions prohibited payment of dividends from unrealised profits. Finally, along with others, the MASB queried whether 'harvest' was correctly defined. For some crops further processing was essential before produce was in saleable form to measure value reliably.

The two most trenchant critics were the **European Commission** and the **Netherlands Council for Reporting** (CAR, 2000). The latter believed the standard should not be released without further consideration of the reliability of fair value measurement and whether recoverable historic cost should also be included as an optional treatment. Specifically, the IASC should prepare a consistent view on fair value accounting as part of a generic accounting model before establishing rules for specific assets or activities. The CAR distinguished between E65 biological transformation during long production asset cycles, *e.g.* for forestry, plantation and extended cattle breeding activities found in other continents, compared to more intensive agricultural activities found in north-western Europe. CAR supported fair value proposals for produce but not for differences in fair value bases for long term bearers. Therefore the CAR favoured recoverable alternative cost and financial capital maintenance concepts in the IASC Framework. Their issue was income reliability *vs.* relevance. CAR was strongly influenced by doubts about expected produce volumes and values being reliably measurable sufficient for income recognition.

The **European Commission's** (EU, 2000) submission was prepared by Member States in the Technical sub-Committee of the Contact Committee on Accounting Directives. It did not support E65 for its conceptual under-pinning, logical consistency and practicability. Amongst its many detailed criticisms were:



- whilst E65 had merit for some agricultural activities the EC could see no merit in applying a blanket approach for all agricultural activities;
- fair value was not always the most relevant measurement basis for biological assets; it relied on erroneous assumptions that
  - efficient markets exist for all biological assets at all times whereas Government quotas, subsidies, tariffs, *etc.*, can invalidate the efficient market hypothesis;
  - fair value determination is assumed available and reliable, without excessive cost;
  - active and liquid markets exist at all stages of biological transformation and growth;
  - growth can be measured sufficiently reliably for inclusion in financial accounts; and
  - all agricultural sectors are sufficiently similar to be accounted on the same basis;
- inconsistency with IAS 18 *Revenue* since the E65 earning process for carrying value changes was regarded as complete at every reporting date;
- concern that E65 was promoting Board and staff views on the validity of fair value accounting and financial performance generally, instead of developing a general standard on reporting financial performance;
- illogical to require fair value accounting for uncertain and volatile transformation processes then record this as operating income with relative certainty and reliability;
- strong practical difficulties in splitting biological assets from the land in which they grow; no logical or conceptual argument for different treatment of the combined assets given valuing land in isolation could be affected by totally different considerations; finally
- *'it is fruitless to engage in dialogue on reliability of fair value measurement given the Board's mindset seems to be that relevance is supreme even if it means reporting unreliable information'*.

### **3.2.8.C. Comments from Developing & Newly-Industrialising Country Members**

Since the proposed standard was originally sponsored for the benefit of developing and newly industrialising countries, submissions from these respondents are instructive.

The **Institute of Certified Public Accountants in Kenya** (ICPAK, 2000) recommended all living animals be valued at fair value, but biological assets and produce be valued at cost. For the latter assets, fair values could not be determined reliably as active markets did not exist for many; *e.g.* few plantations were ever sold. There were no markets for unprocessed or immature crops like coffee, sugar cane, tea and sisal where prices fluctuated widely, up to  $\pm 50\%$  in a year, coupled with periodic Government price interventions. They urged that if cost-based systems were used for other activities the same should apply for agriculture. Finally, they opposed reporting unrealised profits in income because of the difficulty convincing the tax authorities these should not be taxed.

The **Institute of Cost and Management Accountants of Pakistan** (ICMA, 1999) referred to the difficulty with elimination of further processing after harvest in E65. The removal of seeds from cotton-flower, rice husking, fruit grading and packing for quality

determination, and therefore market pricing, were all integral to the agricultural harvest process. Their preference was to recognise 'fair value' only if lower than book value cost.

The **Malaysian Institute of Accountants** (MIA, 2000) agreed with fair value for produce, but not for assets. Reliability would be a problem and fair value determination was impractical and cumbersome.

#### **3.2.8.D. Comments from No-Vote or Abstention Country Member Bodies**

As noted above in Para. 3.2.6., recorded abstentions by the German and Indian delegates with no-votes by the Canadian, Swiss Holding Companies and United States delegates. There was no submission from the Indian/Sri Lankan member organisations although the latter delegate chaired the Agriculture steering committee.

The **Institut der Wirtschaftsprüfer** (IDW, 2000) claimed agriculture was not sufficiently different from other manufacturing operations to justify a separate standard. The IASC had used as justification agriculture's access to sunshine, air and sometimes water as a rationale, but this applied to other industries too. Another concern was inconsistency compared to the IAS 40 *Investment Property* standard where optional 'cost' and 'fair value' treatments were allowed, but 'fair value' was the only treatment permitted for non-realizable biological assets providing services to agricultural activities. Cost information was available which was relevant and reliable. IDW did not favour use of fair values except for monetary assets and financial instruments.

The **American Institute of Certified Public Accountants** (AICPA, 2000) and the **Institute of Management Accountants** (IMA, 2000) made separate submissions. The former did not agree with the basic IASC premise that all biological assets be recognised at fair value, whilst the latter was unconvinced fair value was the right answer, except for produce, and submitted that the project be abandoned. They regarded it axiomatic an entity should sell a product before recording a profit; *'it could even do nothing and still report a profit'*.

In summary the IASC should:

- consider AICPA Position Paper 85-3 as useful in practice;<sup>61</sup>
- limit the fair value model to crops with short term growing cycles, and scope out forest products and other long term biological assets;
- consider the costs and implications for quarterly reporting and disclosures;
- undertake a large-scale Field Test in multiple jurisdictions to determine feasibility and cost-effectiveness; and
- if the Board were still convinced about the E65 proposal, it should consider using a comprehensive income model, rather than reporting movements in the income statement.

The **Canadian Institute of Chartered Accountants** (CICA, 2000) and the **Canadian Farm Business Management Council** (CFMBC, 2000) each made submissions. Both understood the objective but neither could agree with, nor support, the ‘fair value’ system. Each advocated adequacy of a cost-based system as successfully used in Canada. Further conceptual research, debate and justification were required. This had not occurred. It was vital to undertake the field research project. That should have been a prerequisite prior to finalising and issuing E65.

The **Swiss Holding Companies** (I-H, 2000) were adamant ‘fair value’ cannot always be determined reliably everywhere - perhaps relevant in the U.S.A. and Australia - but not in less-developed countries. They did not agree with price elements being recorded in the income statement prior to realisation or being consumed. Consideration should have been given to resolving general performance and income principles for financial reporting before finalising this project; also, a thorough Field Test was essential before proceeding.

### **3.2.8.E. Comments from the Major Accounting Firms**<sup>62</sup>

**Arthur Andersen International** (AAI, 2000) believed fair value was appropriate but E65 needed significant improvements. AAI maintained that the business model for most agricultural entities was to manage to maturity without sales occurring until then.

Therefore the harvest event was the basis for income and profit recognition. Changes in value should be recorded in reserves pending realisation, and then cycling permitted to the income statement. The E65 proposals would add significant burdens on preparers for new systems, valuations and preparation time. In short, costs would exceed benefits. Finally,

<sup>61</sup> Refer also to Section 3, para. 3.4.2.1.

<sup>62</sup> There was no record that KPMG made a written submission.

agricultural land, proposed included within IAS 16, with or without biological assets attached, should be valued at fair value for balance sheet relevance, without a cost option.

**Deloitte Touche Tohmatsu International** (Deloitte, 2000) was generally supportive but had specific concerns that:

- recognition of changes in fair values should not be recorded in the income statement until realisation – and this general exclusion should also apply for non-financial assets;
- the performance statement needed to be expanded as envisaged in the G4+1 (1999) position paper, noting too the precedent in IAS 16, paras. 37+38, for accounting treatment on asset disposal;
- DTTI could only support if fair values could be determined reliably, that is, if convertible into cash, otherwise to record carrying value differences in reserves within equity; and
- E65 needed greatly expanded discussion on the fair value concept and alternative fair value estimation methodologies together with guidance on acceptable practice for establishing fair values for financial reporting.

**Ernst and Young International** (EYI, 2000) supported IASC efforts on an agricultural standard but fundamentally disagreed with E65 proposals. EYI submitted:

- the IASC had not made the case for fair value for non-financial assets;
- the reliability measurement assumptions were seriously flawed;
- the arguments advanced around relevance were misguided - reliability was more relevant;
- the IASC needs to conduct extensive field tests and report back findings to constituents before proceeding further.

In further argument about reliability EYI cited the bull example. It is not the biological growth, maturity and decline of the living animal that is relevant; economic value is determined by revenue from the breeding and servicing capability of each animal. EYI noted that the criteria for IAS 38 *Intangibles* were much more rigorous for valuing assets. IAS 38 required active markets, homogeneous products, willing buyers/sellers and public price disclosure. It was illogical and inconsistent to have a lower hurdle for *Agriculture*. There was lower reliability and surrogates were permissible. There could be wide variations in assumptions including the subjective determination of bearer-asset values attached to land and other infrastructure. Moreover, biological asset homogeneity is lacking due to varying geographical areas, topography, soil, water, breeds, quality, *etc.*, each governing growth and productivity. Finally, market revenues could only be determined reliably at product maturity and sale, not at the outset - nor part-way through.

EYI strongly recommended the IASC to follow U.S.A. and Canadian inventory practice of lower-of-cost or market price.

**PricewaterhouseCoopers** (PWC, 2000) supported the proposal in principle but were concerned about reliability and comparability of reported values. Much more extensive guidance was required, and E65 release was premature ahead of prior decisions on the future of reporting financial performance.

#### **3.2.8.F. Other Critical Themes and Comments**

Other submissions repeated the disagreement with ‘fair value’ proposals. Those respondents submitted all movements should not be credited through the income statement – or, if they were, then realised and unrealised components should be separated; as it was preferable to credit reserves and cycle profits on realisation. They doubted the reliability of the valuation methodology for biological assets. Many disagreed with use of ‘fair value’ for both pre-harvest valuations and as ‘cost’ for inventory. Instead, consistent principles should be determined for valuation bases under the IAS 2 *Inventory* standard.

The **South African Institute of Chartered Accountants** (SAICA, 2000) had decided to expose E65 locally before responding. It advised there was no support for the proposal. Amongst many objections, key issues identified were the lack of qualified accounting personnel in developing countries and inactive and unsophisticated markets so that, given the relative lack of transactional data, historic costs were more meaningful.

However basic support was registered from the Australasian Council of Auditors-General (ACAG, 1998), the Institute of Chartered Accountants in Zimbabwe (ZICA, 2000), the Korean Institute of Certified Public Accountants (KICPA, 2000) and the International Federation of Accountants (IFAC, 2000).

Finally, it is significant that five IASC Board Delegates and five Technical Advisers, with other delegations, signed E65 submissions, refer [Appendix 8A](#). Four Delegates supported E65 proposals with minor amendments, with one not in support; whilst all Technical Advisers expressed critical reservations in principle. This raises questions about potential voting independence and the politicisation of the resulting rule-making process.

### 3.2.9 Summary of Submissions

There appeared to be considerable support for use of fair values for short term crops – but little else. A significant issue was the claim by IASC proponents that E65 provided *relevant* performance measurement, whereas most respondents regarded *reliable* measurement and *reliability* in financial reporting as more important, with recoverable historic-cost a valid option under the IASC Framework. Attention should have been given beforehand to undertaking, and reporting back, the outcome of a full Field Test on E65 proposals and to prior completion of the performance and comprehensive income reporting project, as had been proposed, *e.g.* by addressing the G4+1 paper (1999). In addition, there was a consistent theme in submissions about lack of ‘understandability’ and unacceptability of some of the accounting treatments proposed - reflecting measurement criteria subsequently discussed by Walker and Jones (2003).

It was evident too that respondents identified short-comings with the basis and application of the IASC’s conceptual framework. They referred to the inconsistencies between:

- the definition of income and whether unrealised income should be reported in the income statement, *e.g.* as discussed in Walker (2007, p. 51, citing May 1943);
- inconsistencies in accounting treatment for agricultural land with bearer-assets attached;
- differences between the most recent IAS 38 *Intangibles*, IAS 39 *Financial Instruments*, IAS 40 *Investment Property* standards with yet another basis proposed for *Agriculture*;
- the accounting treatment for income statement performance *vs.* balance sheet ‘wealth’ reporting, and
- whether the resulting financial statements were decision-useful for users and preparers; or met some other standard-setter objective.

There were hints that internal politics intervened ahead of a mutually consistent set of accounting ‘principles’ and treatments. These were addressed subsequently; *e.g.* by Newberry (2003) and Van Cauwenberge and De Beelde (2007). The Comprehensive Income debate is beyond the scope of this study but has practical implications for how bearer-entities were to try and address and distinguish ‘operating performance’ from ‘fair value measurement changes’ when reporting under IAS 41 *Agriculture*.

### **3.3 IASC - Field Test Project**

Camfferman and Zeff had already observed *'in October 1997 when the Board discussed responses to (the) DSOP issued earlier that year...it might have noticed that hardly any reactions had been received from developing countries'* (2007, p. 403). There were only three submissions from 'developing' countries; Argentina, Malaysia and Zimbabwe.

The response to E65 was little better. As identified above, there were responses from the above three member accounting bodies, from the Malaysian and Mexican Standards Boards and their counterparts in Tanzania, Pakistan, and Fiji. However, just one agricultural entity with interests in 'developing' countries, Illovo Sugar Ltd., made a submission and there were only five others from 'developed' countries. The North Group in Australia was the only entity to respond to each of the IASC's DSOP and E65.

Despite earlier references about intending to conduct a Field Test, it was not until its March 2000 meeting that the Board asked staff to *'complete a field test of the practicability of fair value measurements ready for the Board's meeting in June'* (IASB, 2000, June, para 2). The Board was probably influenced by numerous E65 submissions recommending the Board not proceed with the new standard without the benefit of, and report back to respondents on the proposed Field Test. That report-back never occurred; nor was the Field Test Report published.

The writer sought a copy of the Report from the IASB because of repeated references to plans to conduct the Field Test. The IASB supplied a copy of the confidential Board Agenda Paper 7G *Report on the Field Test Findings* for the June 2000 Copenhagen Board meeting (IASB, 2000, June). [Appendix 15](#) contains the full staff summary attached to the Board Agenda Paper, 7G. The additional Agenda Paper 7H was a spreadsheet analysis of responses. This was not supplied so as to avoid identifying those respondents guaranteed confidentiality. The questionnaire was also not supplied. Unfortunately responses cannot be validated by reference to source material.

These summaries should have caused reconsideration as to whether the proposals would achieve a 'high quality' standard and be broadly acceptable to constituents once issued.

The Field Test Project (FTP) questionnaire was posted to 78 agricultural companies, four consultants or accounting firms, one business representative group and one Institute of Accountants. Postal survey invitations were issued by Ms Reiko Yanou, the newly appointed SC Project Manager. Invitees included companies expressing an interest in participating; E65 respondents; and other entities suggested by the IASC Board, SC and staff members (Appendix 15, para 3). *‘Eighteen responses were received, including ten listed companies and eight non-listed companies’* (para 6).

The staff commentary in Appendix B to IAS 41 referred to twenty submissions being received, *i.e.* two unrecorded submissions, possibly from staff, the steering committee or possibly from a Board sub-committee of Technical Advisers.

Table 21 provides a regional summary of recorded responses by agricultural entity type with the latter being evenly spread for the very small sample over each agricultural type.

**Table 21. IASC – Field Test Project Respondents by Agriculture Types**

Companies in.... Agriculture Types	Europe	Australasia	North America	South America	Africa	Asia	Total
Forestry		3	1		1	1	6
Consumable	2	3					5
Bearer		3		1	2	1	7
<b>Total</b>	2	9	1	1	3	2	18

Source: Summary of Respondents to the IASC’s Field Test Project – [Appendix 15](#), page 63.

The questions appear designed to survey from respondents:

- the bases they determined fair values;
- subjective assessment or reliability on use of fair values, applied on a consistent basis;
- their use of fair values for management decision-making; and
- their basis for current reporting whether using cost or fair values for biological produce and assets.

There appeared to be no counter-factual questions surveyed about the merits, or otherwise of other valuation methods; nor did there appear to be any questions about cost/benefit or transitional and operability matters. Accordingly, this may be the reason respondents recorded fuller explanatory comments summarised by staff in Appendix 1 to the Board paper – refer [Appendix 15](#), pp. 74-88. Most expressed concerns on a number of features in the proposed standard. It is open to speculation whether all Board members



assimilated these comments since they do not appear in the agenda report itself. Access to the two ‘missing’ submissions might be instructive and to compare with the Appendix 1.

Responses to the following questions revealed:

1. *bases for determining fair value for biological assets?:*
  - Market prices were used by six companies; NPV by a further six and four replied it was impossible to estimate fair value reliably (Appendix 15, p. 64);
  
2. respondents *subjective assessment or the reliability of their fair values?*
  - on the raw data, eight indicated fair values were reliable and six not reliable. Closer examination shows three participants had ‘no position’ but comments from two indicated this would change to become ‘not reliable’ on a continuing basis;
  - interestingly, two used NPVs to obtain reliable fair values whereas four considered NPVs were or would be unreliable (p. 65);
  - reasons given for lack of reliability, on a continuing basis for regular reporting, were ‘*expressed concerns about subjectivity of fair value measurements arising from assumptions when there is no active market*’ (pp. 65-6);
  
3. *whether biological assets or produce were reported at cost or fair value, currently?*
  - seven of the participants used cost and seven fair value. The figures were identical between the two categories for each of forestry entities, consumable- and bearer-entities categories (p. 71);
  - the contrast between this analysis and the Dowling and Godfrey (2001) summary in Table 7 taken a year before for their 31 entity sample is significant;

As a result, the SC decided to establish a ‘fair value’ hierarchy in the standard (para. 38, p. 72). This emphasised market prices over company-specific present value calculations. Since it appeared problems arose from measuring ‘fair value’ when no market value existed, and differing assumptions were used as well, the SC decided to add ‘*guidance on how net present value calculations should be done*’, (para. 39).

Appendix 15, para. 41, p. 72 discussed whether, following concerns expressed, there should be a ‘reliability exception’ for measurement at cost, where fair value cannot be measured reliably. The SC report did not support the exception proposal. It believed ‘fair value’ and changes in ‘fair value’ were more relevant. Six months later, the Board itself overturned this recommendation in order to obtain sufficient voting majority for approval to issue the *Agriculture* standard.

Perhaps the most telling responses were to the questionnaire which:

asked participants whether they favour the proposal in E65 that, for financial reporting to investors and creditors, all biological assets be measured at fair value and that, at point of harvest, all agricultural produce be measured at its fair value? – Appendix 15, para. 42, p. 73.

The table below summarises misgivings expressed about the utility of the E65 proposal, especially the disparate views from the small sample of consumable- and bearer-entities.

***Table 22. IASC FTP - Respondents Favouring E65 Fair Value Measurements***

	No.	Forestry Entities	Consumable Entities	Bearer Entities
<b>Do Not Favour</b>	10	4	2	4
<b>Favour</b>	7	2	5	-
<b>No explicit position</b>	1	-	-	1
<b>Total</b>	18	6	7	5

Source: IASC’s Field Test Project Table – Appendix 15, para. 43, p. 73.

In support of the above table, staff commentary in Appendix 1 to the Board Agenda Paper contains extensive summaries from respondents (pp. 74-88). These indicate those ‘Not Favouring’ E65 held strong views, from a range of perspectives from each of the entity categories. Taken together, respondents expressed considerable misgivings; whilst those in ‘Favour’ were equivocal, at best.

The Field Test Project was reported to the Board as an agenda paper – probably with an introductory ‘wrap-around’ recommendation - but no further report about the Field Test results could be found in any official IASC news letters, commentaries or articles, notwithstanding that requests to undertake and report back the Field Test findings featured prominently in at least six submissions by E65 respondents.

The staff commentary in Appendix B to the IAS 41 standard simply recorded:

in April 2000, the IASC staff sent a questionnaire to enterprises that undertake agricultural activity to determine the reliability of the fair value measurement proposed in E65 and received 20 responses from 11 countries. In December 2000, after considering the comments on E65 and responses to the questionnaire the Board approved IAS 41 (IASB, 2001, para. B2) [*N.B. Emphasis added*].

This bland statement belied the significant differences in numerous views expressed in E65 submissions and those in the FTP survey, as discussed above. One possibility is that, in the short time available, staff forwarded the FTP survey questionnaire mainly to E65 respondents. Most are likely to have recast or re-confirmed their previous E65 submission.

However, this is not a sufficient explanation for the staff's summary public dismissal of the many constructive comments about and representations made to improve the proposed standard, also recorded in the Field Test Board Paper Appendix 1 commentary.

From a political process perspective, the Appendix B staff commentary attached to IAS 41 provided an explicit example of formally seeking an external *mobilisation* model validation, whilst concurrently adopting the *inside access* model where many external comments seemed not to be accepted if at variance to the insider gatekeepers' preferred outcome (Cobb *et al.*, 1976).

This stance may have strengthened the resolve of those IASC Board voting delegates who sought concessionary changes to be made to the final standard, for instance on the 'reliability exception', against the countervailing and determined politicking from those favouring the project; in particular the Australian delegation and IASC's key insider staff.

## Chapter 4. NEW SGARA & AGRICULTURE STANDARDS

### Introduction

The IASC's IAS 41 *Agriculture* standard was issued sixteen months after the AASB 1037 *SGARA* standard. IASC consideration continued over at least four Board meetings during 2000. The delay occurred to ensure the necessary votes in favour were obtained.

Table 23 provides an overview of the final rule-making stage to issue a new standard.

**Table 23. Agenda Issue Process for New SGARA/Agriculture Standards**

Rule-Making Stage	Elements	Modes of Lobbying	Evidence
<b>Formal Consideration of Agenda Items</b>	AASB issues AASB 1037 IASC issues IAS 41	Submissions to defer AASB 1037. Inter- & intra-Board lobbying and compromise	Board information; Staff 'basis of conclusions'; Journal & other media articles.

Source: Table 9 further modified for the *SGARA/Agriculture* standards processes

The previous chapter discussed the AASB's limited responsiveness to the 46 submissions on the ED 83 *SGARA* exposure draft. The reasons supplied by the Boards and staff insiders was contained in the final section of the AASB 1037 *SGARA* standard, issued in August 1998 (AASB, 1998). The standard was to be effective on or after 30 June 2000. Following further lobbying by practitioners and preparers, AASB 1037A amended the effective date to reporting periods commencing on or after 1 July 2000 (AASB, 1999).

Information on internal IASC politics is derived from a combination of sources. These include comments provided by IASC staff in their Appendix B to IAS 41 *Agriculture* on the 60 E65 submissions; from lobbying activities amongst IASC Board delegates reported by external parties, in particular AASB representatives; and from e-mail communications leading up to the final approval vote. The discussion also provides examples of media coverage and journal articles following issue of the standard.

The IASC Board had been under pressure during the latter half of 2000 to complete the project. Further inter-agency personnel were introduced onto the SC and Board delegations following the Field Test Project to help meet that objective (Appendices 8A and 8B). These staff added to the gatekeepers able to influence political processes.

In the final vote at the IASC's December 2000 London Board meeting the IAS 41 *Agriculture* standard (IASB, 2001) was approved by the bare three-quarters majority following four country delegation no-votes or abstentions.

Completion of this project was the final act of the IASC before it was dis-established shortly after conclusion of the London meeting. IAS 41 was the final standard issued by the IASC. As further timetable pressure on the IASC Board, delegates were aware that had the standard not been approved at that meeting, the formal consideration processes would have had to restart in 2001 under the auspices of the newly-created IASB. As a result, some of the conditional support in E65 submissions was compromised arguably by inadequate consideration and an incomplete report-back process.

#### **4.1 Australia – Issue of the AASB 1037 SGARA Standard**

AASB 1037 was issued by AASB Chairman, Ken Spencer, on 6 August 1998, by authority of Section 334 of the Corporations Law with an operative date for financial years ending on or after 30 June, 2000, but with earlier application permitted (AASB, 1998). The Boards issued two standards with AARF support. The AASB issued AASB 1037 and the Public Sector Accounting Standards Board (PSASB) issued AAS 35:

- *AASB 1037* was mandatory for GPFR preparation and reporting by companies, disclosing entities and registered schemes regulated by the Corporations Law;
- *AAS 35* was issued by the PSASB and applied to non-corporate reporting entities in the private and public sectors not required to apply AASB standards.<sup>63</sup>

There were no mutual recognition or conformity requirements to meet, since neither the IASC, nor New Zealand, had issued an agriculture standard. AASB 1037 was therefore the first formal general purpose reporting standard for agriculture outside North America.

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<sup>63</sup> All references and discussion relate to AASB 1037, except where reference to AAS 35 is necessary.

One reason given was that '*notwithstanding Policy Statement 6, International Harmonisation Policy*', the Boards had decided to press ahead due to '*uncertain timing for the IASC project and urgent need for guidance for Australian entities that control SGARAs*' (AASB, 1998, p. 23). The Boards did not elaborate on these reasons but pressure was apparently being applied by State Governments onto the PSASB/AARF to facilitate forestry corporatisation and privatisation.<sup>64</sup>

The preamble also noted '*the Boards will continue to provide input to the IASC as opportunities arise and in the interests of harmony between the Australian Standard and an IASC standard on Agriculture*' (*ibid.*, p. 23).

There was also another possible reason for accelerating issue of the AASB 1037 standard prior to the IASC standard, caused in part by continuing delays with the IASC project.

The AARF support role to the Boards, was destined to change and existing AARF staff could potentially be re-assigned. This was because of the proposed *Corporate Law Economic Reform Program* (CLERP-1, 1997; Jones *et al.*, 2000; Stoddart, 2000). In March 1997, the Federal Government announced CLERP-1 implementation on 1 January 1999; but subsequently, it was deferred by a year because of lobbying pressure (Brown and Tarca, 2001). In the event, those most closely associated with the SGARA project, Robert Keys and Angus Thomson, transferred to the new-AASB holding senior technical staff positions.

The changed CLERP-1 structural responsibilities are described in [Appendix 5](#) for accounting standards and reporting relationships pre- and post-1st January 2000.

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<sup>64</sup> As revealed in numerous interviews and as confirmed by Angus Thomson, AARF Technical Director, in an email communication in November 2002 for the writer's Delahunty Project.

#### 4.1.1 Commentary on AASB 1037 Content

AASB 1037 Clause 1 '*Application*' confirmed the standard applied to any reporting entity required to present financial statements in accordance with Part 2M.3 of the Corporations Law where they purport to be a general purpose financial report (AASB, 1998).

The scope applied to all SGARAs - other than those '*held for the primary purpose of aesthetics, heritage, ecology, the environment or recreation [and to] exclusive rights over SGARAs through leases or similar arrangements over SGARAs as if those rights are themselves SGARAs*'. That is, the standard applied to '*SGARAs that are held primarily for profit [whether] for sale in their own right or held to generate produce for sale*' (*ibid.*, Section 2, p. 2). AASB 1037 prevailed in the event of conflict with any other standard. However, the standard excluded any accounting treatment for future sales price or delivery hedging contracts for non-living SGARA produce.

The scope and purpose of AASB 1037 prescribed:

- a) SGARAs be measured at net market values (at each reporting date);
- b) increments/decrements in NMVs be recognised in the profit and loss statement in the financial years (these) occur;
- c) the NMV of the non-living produce extracted from SGARAs (less the costs of extraction) determined immediately after it becomes non-living be recognised in the profit and loss statement in the financial years in which the extraction occurs;
- d) the cost of the non-living produce of SGARAs is deemed to be the NMV of the non-living produce immediately after it becomes non-living; with
- e) specific disclosures be made in respect of SGARAs (*ibid.*, Section 4.1, p. 3).

Each of these scope elements was further expanded in commentary elaborating on the Boards' decisions and clarifying matters arising from selected submissions. The discussion below identifies the principal items.

The Recognition criteria were that a SGARA must be recognised when:

- a) it is probable that future economic benefits embodied in the SGARA will eventuate, and
- b) the SGARA possesses a value that can be measured reliably' (*ibid.*, Section 5, p. 3).

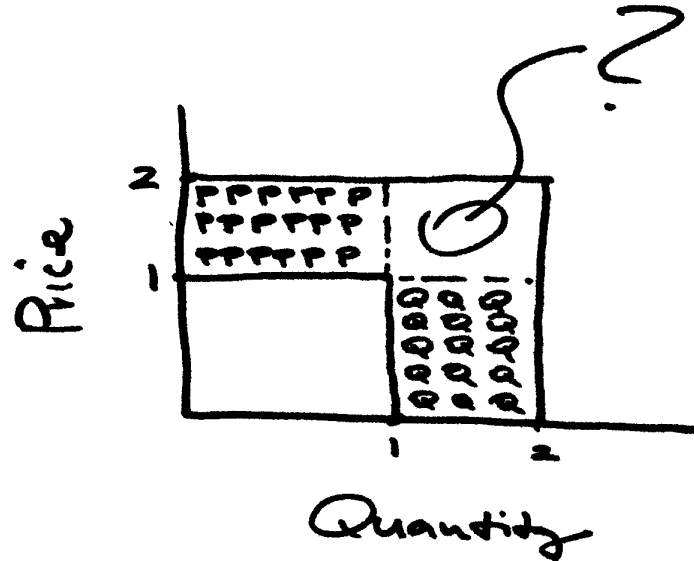
The commentary suggested '*it would be extremely rare that SGARAs held primarily for sale or otherwise to generate profit could not be measured reliably*' (*ibid.*, Section 5).

The discussion below explains the AASB's SGARA concept. In addition, the Boards' comments are recorded with alternative or unresolved views from ED 83 submissions:

**a) Basis of Measurement** (*ibid.*, Section 5.2, pp. 4-6):

- '*measuring SGARA at current value ensured the effects of both biological change and price were recognised*'. This was primarily directed at forestry since the Boards claimed the separate elements were difficult to identify reliably – even though this had been long-established practice for livestock accounting. The AARF view on the difficulty in attributing price and volume effects for forestry over two periods is recorded in this diagram prepared by Angus Thomson.

**Figure 5. Impossibility of Ascribing SGARA Price and Growth Value Components**



Source: E-mailed diagram from Angus Thomson to the writer sent on 28 November, 2002

- NMV was the amount expected from disposal in an active and liquid market, after deducting costs associated with disposal. This provided a farm-gate valuation as the relevant comparative basis for '*assessing stewardship of the entity by indicating the effects of decisions to buy, sell or hold SGARAs...separate from management's own intentions*' for use or disposal. This implied for users' benefit that a spot price subject to temporary supply/demand aberrations was superior for performance reporting purposes, compared to any alternative view by management of appropriate prices, and risks, involved in managing SGARAs for optimal results;



- ‘market prices observed in active and liquid markets often will be available for SGARAs at all stages of their maturity’. This reference related to livestock. It completely over-looked submissions from forestry and bearer-SGARA entities;
- however, there could be instances where there was no active or liquid market for disposal of a SGARA, in which case judgements must be applied balancing *reliability with relevance*, and *vice versa*, using other surrogates instead. These might be any of the best asset or product price indication from another market, or related similar assets or products, or recent relevant historical prices;
- two examples were supplied to illustrate SGARA measurement bases:
  - for an apple orchard: to obtain the NMV of the apple trees, the current orchard NMV should be used as the base, from which is deducted the underlying land valuation at its best-use value. If the alternative-use land value were to exceed the orchard NMV, the apple trees would have a nil carrying value for reporting purposes. Another example given was where a forest managed for [say] a hardwood clear-felling regime would be required to use pulp-wood tree values, or *vice versa*, whichever was the higher;
- if a DCF valuation technique were used to determine a surrogate-NMV, the discount rate should be a ‘*current market-determined rate which reflects the risks associated with those assets...excluding outflows for financing...and taxation...and for replanting obligations*’;
- this over-looked the reality that post-tax cash effects for tax timing and fiscal incentives would be reflected in an arms-length net market value. Furthermore, exclusion of tax cash outflows in the DCF calculation would over-state balance sheet asset values but with partial offset for a deemed deferred tax liability. There was also the possibility in some cases that deferred tax entries were double-counted since a carrying value change recorded through the income statement, unrelated to the underlying tax base, would also require a further notional income tax charge/credit under IAS 12 to obtain the reported net profit/loss;<sup>65</sup>
- however, cost may be used where little biological change had occurred or uncertainties render NMV determination unreliable or irrelevant; or ‘*where the time between incurring costs and determining NMV (requires) assumptions about yield and market prices [which] cannot be made reliably*’.

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<sup>65</sup> This still persists. The IASB initiated ED IAS 12 to help remedy the defect. It proposes to include further amendments to IAS 12 in a future Improvements Project, when agenda time permits.

**b) Recognition of Revenues and Expenses** (*ibid.*, Sections 5.4-5.6, pp. 6-7):

- the basic concept for the standard was ‘*revenue is typically realised from a SGARA by either selling the SGARA or extracting non-living produce from the SGARA*’, that is, a typical arms-length sale at harvest with risk transfer at point of sale.  
But this did not reflect the business reality for some agricultural sectors, *e.g.* viticulture or sugar, where security of supply from own-produce is integrated as a business operational quality and risk management control objective through the entity’s entire supply chain from land operation to end-consumer;
- thus, revaluing *produce* to NMV immediately prior to ‘*disposal – being the net disposal proceeds – [means] no gains or losses result...therefore proceeds from the sale of SGARA are not recognised as revenues*’ rather, as changes in the NMV carrying-value, net of related extraction expenses accrued in the reporting period;
- harvest or extraction value becomes the essential measurement and performance basis for asset and produce. Un-harvested produce attached to a SGARA asset, *e.g.* grapes on a vine, would be a growth element within the bearer-asset value. On harvest, the asset NMV reduces accordingly. However, there was no discussion on the implications for Interim reporting raised in submissions;
- to be consistent with the requirements of the existing AASB 1004 *Revenue* and AASB 1019 *Inventory* standards and in an attempt to eliminate double- or triple-accounting of revenue the SGARA accounting conceptual basis may be described as follows from the AASB explanations:
  - revenue accrues to the growing SGARA asset prior to harvest;
  - expense of harvest is a diminution of produce NMV at the time of harvest;
  - the cost of the non-living produce is deemed for inventory purposes to be its NMV immediately after it becomes non-living; so that
  - net realisation proceeds from sale of non-living produce equal the deemed NMV cost of inventory arising from harvest (AASB 1998, Sections 5.4 – 5.6).

This assumed an arms-length sale had occurred. Appendices to the AASB 1037 standard provided examples showing recommended accounting entries and presentations. They exceeded the length of the text of the standard, without satisfactorily resolving the cost-of-sales issue and other adjustments required when inventories were not sold in the same reporting period or continue in inventory as own-produce operational inputs within an integrated entity’s operations.

**c) Presentation** (*ibid.*, Section 6, p. 7):

- SGARAs were to be identified as separate assets in the balance sheet because *'their "living" characteristic makes them unique'*.

The consequence was that a SGARA attached to a non-SGARA was required to be dis-aggregated and separately accounted because each was subject to different reporting standards, *i.e.* the equivalents of IAS 16 and IAS 41;

- changes in SGARA asset carrying values were only to be reported within the income statement and not separated between income and reserves, nor between realised or unrealised components.

**d) Disclosures** (*ibid.*, Section 7, pp. 7-8):

Extensive disclosures were mandated; some in excess of disclosures for other industry reporting entities; for example, separate disclosures were envisaged for:

- plants and animals, per DP 23, including lease and other similar arrangements;
- nature, extent and description of external restrictions on use impinging on NMV;
- where NMV was not based on market prices: the method used to determine NMVs; any significant assumptions used; whether based upon directors' or independent valuer's determinations, and, if the latter, the valuer's name or firm;
- the carrying value change in NMVs attributed to each of plant and animal SGARAs and the difference between the opening carrying value and that at time of extraction recorded in the profit and loss account, including the method of determination used;
- although it was not obligatory, entities were encouraged to provide appropriate information about future prices, yields, costs, timing of harvests, discount rates and exchange rate assumptions used in measuring carrying amounts, since such information would be *'useful to users of financial reports'*.

**e) Transitional Provisions** (*ibid.*, Section 9, p. 8):

Differences between carrying value and NMV at transition date were required to be held in retained earnings and not adjusted to the income statement as was mandatory after transition.

There was no change to ED 83 provisions despite specific submissions on the unfairness for long term agricultural entities. Objection remained that any economic surplus on growth, previously credited to reserves, became at transition 'locked into' reserves within equity. These were then unable to be cycled to the income statement on subsequent realisation and therefore were unavailable for distribution as dividends from reported profits – unless by innovative use of other transitional provisions.

**4.1.2 Development of the New Standard** (*ibid.*, pp. 23-5):

Attached to the standard – but not officially part of it - was an additional commentary identifying differences from ED 83; principal features retained in the standard and the Boards’ summary of some of the replies expressed in submissions on ED 83.

**a) Noteworthy Differences from ED 83**

- ED 83 proposed a single SGARA balance sheet classification. However AASB 1037 required SGARA reporting separation into current and non-current categories in order to comply with IAS 1 *Presentation of Financial Statements* requirements;
- the Boards accepted that some of the proposed ED 83 disclosures were unduly onerous; for example, the proposed disclosure of actual physical quantities, *i.e.* for the number of trees in a forest, vines in a vineyard. Accordingly disclosures were modified to ‘*an estimate or relevant information of physical SGARA quantities*’;
- the Boards however encouraged fulsome disclosures for users’ benefit; and
- ED 83 provided no prescriptive specification about changes in NMV carrying values because of the expectation equivalent information would be contained in AASB 1005 *Reporting by Segments* and AASB 1034 *Information to be disclosed in Financial Reports*. Instead, the Boards decided, for completeness, to include all SGARA accounting and reporting requirements within the one standard.

**b) Principal ED 83 Features Retained in AASB 1037**

These were summarised as the complete basis for conclusions for the new standard:

SGARAs are required to be measured at net market value, and a change in that value is to be recognised as a revenue or an expense in the profit and loss statement in the financial year in which change occurs. The Boards believe that net market value best reflects the future economic benefits embedded in SGARAs because it captures the value of biological transformation which is not adequately reflected in historical costs. Although historical costs may be similar to current value at acquisition and some time thereafter, over time it would normally differ materially from that value, particularly if the SGARA has a long maturation period. Additionally certain SGARA, such as native forests, may not have an associated historical cost. Entities applying historical cost measurement of those SGARAs would therefore omit certain valuable assets from their balance sheet. Furthermore, using net market value enables the profit and loss statement to reflect a more relevant measure of the periodic performance of an entity that controls SGARAs than is the case using historical costs (*ibid.*, p. 24).

### c) Unresolved Issues

A number of issues contained in submissions were ignored.

In the DP 23 SGARA biological accounting taxonomy SGARAs related either to ‘plants’, with trees as proxy, or ‘animals’, with livestock as that proxy. The standard included references to ‘plant’ and ‘animal’ categories in the discussion sections.

However, the effect of the standard was to go further. AASB 1037 was formulated as an omnibus standard for all agricultural sectors. There was no distinction between the essential fundamental differences between consumable- and bearer-SGARAs – except in note disclosures. After the numerous submissions, further adverse reaction was inevitable from bearer-SGARA entities and from academic, analyst and media commentators.

Concerns expressed about the accelerated timing of AASB 1037 possibly related to the CLERP-1 framework proposals. That framework was the basis for establishing the AASB as the principal standard-setting body with the presumption that the AASB should no longer issue *‘its own standards and instead move quickly to adopt international accounting standards issued by the IASC’* (Brown and Tarca, 2001, p. 280), citing also:

from 1 January 1999, the AASC should issue identical exposure drafts of standards for public comment to those issued by the IASC with the objective that final standards issued by the AASC would be consistent with Australian law and would be the same as those issued by the IASC, unless the Government, on advice of the FRC, determines that to do so would not be in Australia’s best interests (CLERP-1, 1997, p. 2).<sup>66</sup>

The new standard-setting structure revised the process for developing accounting standards. CLERP-1 required the AASB to conduct a cost/benefit analysis prior to formulating a new standard, unless it was derived from an international accounting standard (*ibid.*, Section 213.1); and, a cost/benefit analysis of a proposed international accounting standard must be conducted before commenting on or proposing to adopt one, but only if reasonably practical to do so (Section 213.2).

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<sup>66</sup> N.B. The AASC was subsequently renamed the AASB, refer also to [Appendix 5](#).

It is probable the Boards/AARF insiders decided on a pre-emptive strategy to issue the SGARA standard prior to issue of the IASC's exposure draft, and before the CLERP-1 was enacted so as to avoid, or minimise the transitional impact of its requirements. The AASB could then retain the initiative for primacy of an already-approved AASB 1037 standard in eventual lobbying with IASC voting delegates.

During the writer's first Field Trip in 2002, some interviewees commented upon this when recounting the urgency to issue AASB 1037 in advance of the IASC standard (Milne, 2004).

In response to a direct query, the AARF advised there was no cost/benefit analysis done at that time because there was no legal requirement to do so for AASB 1037. However, had the AARF undertaken a cost/benefit analysis, the perceived benefit would have been to provide better information sooner. These analyses would not be quantitative, always qualitative.<sup>67</sup>

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<sup>67</sup> Angus Thomson email to writer in 28 November 2002. The final sentence referred to *Figure 5* on p. 174.

### **4.1.3 Publicity on Release of the AASB 1037 SGARA Standard**

Robert Keys as the AARF ‘Senior Project Director – Accounting’ published an article in the *Australian Accountant* heralding the new standard (Keys, 1998b, Oct.). This discussed the Boards’ answers to those ED 83 objections based upon comparisons with historic costs. Keys repeated the summary in Para. 4.1.2.b. The emphasis of the new standard was on a SGARA’s living nature as the distinguishing characteristic compared to other property, plant and equipment. Keys argued although there may be perceived similarities, a SGARA, *e.g.* a vine, was fundamentally different from a machine. Thus he maintained the importance of separating an integrated SGARA from its non-SGARA asset so as to retain the ‘*defining scope of the standard*’. The remainder of the article covered NMV criteria, recognition, non-living produce, and presentation and disclosure issues.

In addition, he published a longer article (Keys, 1998a, Oct.). It repeated much of the content and the Boards’ arguments discussed above. However, for the first time, a number of critical media articles appeared in *The Accountant* in London (Anon., 1999, April); by commentator Leon Gettler syndicated respectively to *The Age* and *Sydney Morning Herald* (Gettler, 2000a, July; Gettler, 2000b, July); and a fourth by David Moodie, an Adelaide free-lance journalist (Moodie, 2000, Dec.).

The *Accountant* article (Anon., 1999a, April) and a Gettler article (Gettler, 2000a, July) are reproduced in Appendix 16 to reflect contemporary media comment. The sub-editors’ provocative headlines matched the content. The reported adversarial role of Southcorp Ltd. is evident in Gettler’s article and is consistent with Southcorp’s submissions to the AASB, the IASC and its Field Test participation.

The defensive remarks reported by Kenneth Spencer, AASB Chairman, to the charge ‘*Australia was [needlessly] leading the world*’ are significant too. They may have reflected the eventual outcome of the standard-setting process with the IASC, but this was not the case when the articles were written in mid-1999. Moreover, Spencer supplied two *non-sequiturs* as beneficial reasons for supporting the new standard; but only applicable to agricultural entities, and not available for any other entities or industrial activity.

#### **4.1.4 Deferral of AASB 1037 Implementation Date**

AASB 1037 was issued operative for financial years ending on or after 30 June 2000.

Immediate submissions from preparers and practitioners claimed there was insufficient time to develop new accounting and computer systems to capture all the new information required for AASB 1037 disclosures and reporting. Other concerns included lack of transitional provisions, application of capitalised interest costs and '*adoption of net present value techniques for determining the NMV of trees in forests*' (PWC, 1999, July). These claims were examined and found reasonably justified by Herbohn and Herbohn (1999), at least for forestry entities, and more generally by Dowling and Godfrey (2001).

The Boards '*decided not to amend the standards but rather to allow entities additional time to address these concerns by deferring the operative date for 12 months*' (PWC, 1999, July). In July 1999, the Boards issued AASB 1037A operative for reporting periods commencing on or after 1<sup>st</sup> July, 2000 (AASB, 1999), with earlier adoption encouraged. In reality, the deferral was for only 6 months. Entities' interim reporting on 31 December 2000 had to respond to the new standard, including re-statements for prior periods.

#### **4.1.5 Summary**

When AASB 1037 was issued in August 1998, the Boards and the AARF had not managed to assuage concerns of many ED 83 respondents, especially bearer-entities, with the explanations given in commentaries on the standard. Therefore critical comments followed when reporting entities published their first Interim and Annual Reports.

Meanwhile, the IASC had to complete work on and issue of its IAS 41 standard. The new *Agriculture* standard would then have to transfer to Australia for exposure by the AASB for convergence as a harmonised international standard. The exposure draft was issued with a concurrent post implementation review into experience with the AASB 1037 standard. These two stages offered further opportunity to submit practical criticisms and supply further recommendations. Each is developed in Sections 5 and 6 respectively.



## **4.2 IASC – Issue of the IAS 41 ‘Agriculture’ Standard**

The IASC approved issue of IAS 41 *Agriculture* at its last meeting in London in December 2000. It took four Board Meetings after E65 approval to consider aspects of the project; revisit areas of concern; negotiate optional accounting treatments and finally reach Board delegates’ three-quarters voting majority sufficient for formal approval.

During this period, changes to the SC membership occurred. The discussion below outlines principal matters being reported at respective Board meetings, including lobbying activities, and concludes with elements that differed from E65 and new features introduced for IASC’s accounting for *Agriculture*. This is followed with publicity surrounding release of the standard.

### **4.2.1 Changes in IASC Key Insiders**

Warren McGregor ceased to be a Board Technical Adviser during 1999. Liesel Knorr was replaced in September 1999 as Technical Director by James Saloman originally with the Ontario Securities Commission and seconded from PricewaterhouseCoopers in Toronto.

Appendix 8A identifies the Board and Technical Adviser country delegates and Appendix 8B the Steering Committee membership for this final agenda consideration stage. Ms Reiko Yanou, from Deloitte Japan, was appointed Project Manager to undertake much of the follow-up work on behalf of the Board, and for Paul Pacter prior to his retirement from the IASC in June 2000. S. Dedman, from the U.K. was appointed a committee member. Robert Keys was noted as a seconded observer from the AASB.

### **4.2.2 Political Processes at Respective Board Meetings**

The previous chapter referred to the need for one out of the five no-vote or abstaining delegates to change their E65 voting position for the standard to obtain formal approval. The political processes and deliberations were reported back to Southcorp Ltd. by an

Australian able to attend Board meetings.<sup>68</sup> The full e-mail advice reported to Southcorp on 3 November 2000 outlined progress:

- at the Copenhagen meeting, in June 2000, it was proposed that consumable SGARAs be measured at net realisable value and bearer SGARAs be valued at net fair value, with gains/losses for both through the P&L. A cost alternative was to be permitted, but of very limited application, *e.g.* only where it could clearly be demonstrated that fair value measurement was inappropriate or impractical. The first was a variant to E65;
- at the Tokyo meeting, in October 2000, this consumable/bearer distinction was removed, in line with E65, with the net fair value the proposed measurement basis. This version did not get the required 12 'in favour' votes out of 16. The U.K., Australia and some others were trying to get the cost alternative removed. The proposal has therefore been listed as the main agenda item at the December meeting in London, which will probably be the last for the current Committee;
- Germany, Switzerland, the United States, Canada and Japan are the five countries who are currently not supporting the proposals. Some, *e.g.* the U.S.A., are principally opposed because they do not support revaluations in general, despite the individuals involved possibly personally supporting revaluations, and others, *e.g.* Germany, are opposed because they believe such revaluations should not go to P&L; the other 11 countries seem happy to proceed with most aspects of the revised standard;
- the Australians have been instructed to support the standard regardless of any personal views. Ken Spencer's main brief is to try to get an international standard that is compatible with AASB 1037;
- it was line-ball as to whether approval happens at the London meeting. If it does not, it has been suggested that it will be re-submitted to the new committee structure in 2001 and may be approved at that time.

On 19 December Southcorp was advised on the outcome of the London Board meeting:

- the IASC passed IAS 41 thereby adopting fair value accounting for biological assets and produce harvested from them from 2003, with gains/losses to P&L. Only in exceptional circumstances will the cost basis be permitted;
- IAS 41 received 12 votes in favour as required, with 2 against, Germany and the Swiss, and two abstentions, U.S.A. and India/Sri Lanka. Japan and Canada ended up voting in favour. It was thought that U.S.A. or India/Sri Lanka would have changed their vote to being 'in favour' had it been necessary for approval, as it was accepted that IASC 'needed' to pass it.
- IAS 41 was viewed as being broadly consistent with AASB 1037. The new IASC will consider issuing further guidance on implementing IAS 41 in due course;
- apparently the EU will be requiring all European companies to comply with IASC standards around 2003, so these standards will have greater importance. How the U.K. will be impacted was uncertain. The relationship between IASC standards and the US GAAP was also a major issue, particularly for European companies with US-listings. The new IASC will be working on these issues.

Camfferman and Zeff corroborated the internal Southcorp correspondence:

the main difference with the IASC's evolving approach was that the Australian delegation staunchly, and successfully, defended their own standard in the IASC board from (ED 83) onwards. As acknowledged by Bryan Carsberg, both E65 and IAS 41, *Agriculture*, were very similar to AASB 1037. Conversely, the AASB pointed to the adoption of the Australian standard to defend its approach against criticism coming from the Australian corporate sector.

<sup>68</sup> Supplied by D. Jeffries, General Manager - Accounting, Southcorp Ltd. for the Delahunty Report

For IAS 41 to be approved, a reluctant Canada had to be persuaded by several changes which left the overall approach to E65 intact. The changes included an exception for biological assets whose fair value cannot be measured reliably. What also helped, presumably, was that the final vote was taken at the last board meeting. There was a strong feeling that, in the light of the World Bank grant, it would not do for the IASC to leave the project unfinished. The other delegations voted as on E65, with the result IAS 41 passed with the smallest possible majority (2007, pp. 403-4).

#### **4.2.3 Basis for Conclusions Commentary on IAS 41 Content**

A 'Basis for Conclusions' supporting IAS 41 was:

prepared by the IASC staff and [was] not approved by the IASC Board. The Appendix summarised the Board's reasons for:

- a) initiating and proposing...a standard on Agriculture; and
- b) accepting or rejecting certain alternative views. Individual Board members gave greater weight to some factors than to others (IASC, 2001, Appendix B, pp. 35-61).

The 'Basis for Conclusions' followed a format of presenting many of the submissions made along the lines that:- E65 made certain proposals but some respondents 'argued', 'believed', 'may think', 'indicated' or 'opposed' various propositions. The Board then 'decided', 'rejected', 'concluded' or 'commented' that the standard required particular accounting treatments. These descriptions reinforced evidence of lobbying consideration and acceptance or denial by 'insiders'.

There was scant recognition that these conclusions were judged from first principles or from the conceptual framework; rather to meet the objective of developing standards *relevant* for GPFRR of all businesses. It was this perceived disconnect of relevance vs. reliability of accounting treatment which had been the tenor of many submissions.

Following the insistence of the Canadian delegates, the compromise added to the standard was ***Inability to Measure Fair Value Reliably*** (*ibid.*, paras. B. 34-7).

This allowed rebuttal to the presumption 'fair value' could be determined reliably on initial recognition where market-determined prices or values were not available, or for which alternative estimates of fair value were unreliable. In that case, the biological asset should be measured at cost, less any accumulated depreciation. However, once 'fair value' measurement was reliable, the biological asset was then to be measured at fair value, less point of sale costs. This was expected to occur due to future biological transformation. In

the meantime, extensive additional disclosures were required as to why ‘fair value’ could not be measured reliably. The standard did not permit the rebuttal presumption to reverse.

There was a *Summary of Changes to E65* (*ibid.*, Para B.82, pp. 58-61). These were:

- a reliability exception on initial recognition with measurement at depreciated cost pending such time as fair value can reliably be determined, with associated special disclosures;
- IAS 41 now required point of sales costs to be deducted from fair value, previously excluded;
- E65 referred to net realisable value as a permitted valuation; now excluded because not a market-determined value;
- where market-determined values were not available for an asset in its present condition, then an entity should use the NPV of expected net cash flows; but with guidance supplied in the standard on present value calculations;<sup>69</sup>
- unlike E65, IAS 41 indicated that fair value of an asset or produce must not be adjusted because of the existence of a sales contract;
- any gain or loss on initial recognition to be included in the current period net profit or loss;
- costs of producing or harvesting costs should be charged to expenses as incurred;
- IAS 41 did not prescribe how to account for subsequent expenditures on biological assets;
- conditional Government grants related to biological assets to be measured at fair value, less point-of-sale costs, and grants not to engage in specified agricultural activities, are to be measured as income when specific conditions attaching to the grant are met; but where IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* is applied these are measured at cost less any accumulated depreciation or impairment losses;
- extensive new disclosures were prescribed;
- IAS 17 *Leases* was amended so that IAS 17 should not be applied to measurement by lessees of biological assets under a finance lease; nor to lessors of biological assets being leased under an operating lease. Each should measure respective leases under IAS 41 but also present and disclose the leases under both standards.

Finally, the key definitions applicable to IAS 41 comprised:

- ***agricultural activity*** is the management by an enterprise of the biological transformation of biological assets for sale, into agricultural produce, or into additional biological assets;
- ***agricultural produce*** is the harvested product of an enterprise’s biological assets;
- a ***biological asset*** is a living animal or plant;
- ***biological transformation*** comprises the processes of growth, degeneration, production, and procreation that causes quantitative changes in a biological asset;
- a ***group of biological assets*** is an aggregate of similar living animals or plants;
- ***harvest*** is the detachment of produce from a biological asset or the cessation of a biological asset’s life processes (*ibid.*, para. 5, p. 11).

After five years and except for the management criterion, IAS 41 definitions were similar to the original *Project Brief* criteria and UNE definitions, with continued emphasis on biological assets that were living and which undertook biological transformation.

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<sup>69</sup> The guidance in IAS 41:21 proved to be unsound. It was subsequently amended by the IASB in 2008.

#### 4.2.4 Publicity after IAS 41 Release

First reports emerged in the 2001 New Year that IAS 41 had been approved by the IASC at its December meeting with a brief description of the principal requirements (Anon., 2001, Feb.). Further elaboration was provided by David Cairns (2001, April), a former Secretary-General for the IASC and now a consultant on international financing issues. That article identified *'the IASC undertook this project primarily to meet developing country needs. For this reason, the World Bank provided funding of US\$ 650,000 for the project'*. Cairns had negotiated the original grant from the World Bank.<sup>70</sup>

As was customary, a comprehensive discussion on IAS 41 was published by the IASC Project Manager, Ms Reiko Yanou. It traversed all aspects of and rationale for the principal issues (Yanou, 2001, April). Separately, Reyaz Mihular, Chairman of the Agriculture SC, also published comments (Mihular, 2001, April). In particular, he discussed concerns about reliability of fair value measurement for some biological assets; especially for those with long growth periods where arguments were advanced on the subjectivity of assumptions underlying net cash flow calculations.

Commentaries were published in Australia, New Zealand, India, U.K. and Canada.

In Australia, it was confirmed that IAS 41 and AASB 1037 essentially prescribed the same principles, although differences in terminology and disclosures now existed. The particular difference identified was the IAS 41 definition of *'fair value, less estimated point-of-sale-costs'* whereas AASB 1037 had referred to net market value which *'means the amount which could be expected to be received from the disposal of the asset in an active and liquid market after deducting costs expected to be incurred in realising the proceeds of such a disposal'* (Dixon, 2001, March) [*N.B.* Emphasis added]. Thus the IASC had not been responsive to AASB's representations on this particular matter.

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<sup>70</sup> The original IASC reported figure was US\$531,000 (IASC, 1996c).

Publications in New Zealand (McDonald and Thompson, 2001, April) and India (Murali, 2001, July) identified that local institutes would now be required to harmonise with the IAS 41 standard. However, the latter article expressed some cynicism about the role of the local Institute, which had taken six months to report the effects of IAS 41 and the relevance of an agriculture standard when there were other much more pressing accounting issues, so that *'next could be an accounting standard for dinosaurs'*.

An article from the United Kingdom reported that the Accounting Standards Board (ASB) was conducting research after the European Commission's proposal that all listed companies accounts should comply with IAS' by 2005 in order to improve the harmonisation of accounting in the single market (Anon., 2001, March).

In July questions were asked about how ready British farmers were for IAS 41 (Butler, 2001, July). In particular, implications of IAS 41 inventory fair value measurement and incompatibility for taxation determination purposes under BEN19, Inspectors Manual IM229, since *'taxable profits are increasingly reflecting accounting profits under UK-GAAP'*. Either tax law would have to change, or ASB refrain from adopting IAS 41. The Institute of Chartered Accountants in England and Wales was reported to be considering its position after initially opposing early adoption of international accounting standards.

In similar vein, there were critical remarks by Professor R. Paterson from Glasgow about the IAS 41 *'Trojan Cow'*. This *'chips away at the realisation principle which remains the predominant basis for performance reporting, but is increasingly under threat by standard setters who hanker after a universal fair value model...and will cite this standard [in future] as a persuasive precedent'*. Paterson discussed the pros and cons of the standard and observed that if farming is defined as the management of biological transformation, then value is created by the farmer doing this well, just as in other businesses, and that *'value is actually created by many intermediate activities and is only crystallised by sales'*. However, although Paterson might have expected consternation in the farming community over the standard, he identified that in reality it would have little impact because few farmers were then subject to IAS' anyway (Paterson, 2001, Nov.).

In Canada, there was a comprehensive article in the Chartered Accountants magazine about the development of and reasons for farm management accounting practice in Canada, and in the United States, with its deemed more relevant individual sector-based accounting pronouncements. One effect of IAS 41 would be to standardise practice and procedures for all farm sectors so that *'consistent and accurate measurement of operating results on a standardised basis allows the producer to make informed business decision'*. Kinnell noted *'the Canadian Accounting Standards Board has no approved project to reconsider GAAP (valuation principles) for inventories or capital assets'* (2001, June). Kinnell was a signatory to the CICA E65 submission recommending against adoption of the proposed IASC standard (CICA 2000).

### **4.3 Summary**

The IASC's Agriculture project was complete. Camfferman and Zeff noted *'the standard was a fitting finale for the IASC, as it became a showcase of the IASC's move towards a balance-sheet-oriented approach based on fair value measurement'* (2007, pp. 401-2).

The technical fair value components of the new standard had not accommodated concerns in lobbyists' submissions. Anomalies remained; in particular for bearer-entities. Final consideration had been compressed into a relatively short period so that unresolved items from exposure draft lobbying and Field Test findings remained unreported.

Source material revealed inter-agency and internal gatekeeper lobbying in order to obtain the minimum IASC three-quarter's voting approval. This was achieved by compromise on the 'reliability rebuttal presumption' rather than adherence to the conceptual framework. In hindsight, the rule-making process was deficient. The FTP was conducted too late to effect reconsideration. It should have preceded issue of E65 so results could be considered prior to its release. Many submitted the project would also have benefited from more work to ensure the 'fair value' methodology was applied consistently across other recent standards (e.g. IAS 39 and IAS 40) rather than permitting inconsistent piece-meal developments. Prior to issuing IAS 41, further work should also have included completion of the valuation criteria and the G4+1 (1999) comprehensive income performance measurement projects.

## Section 5. IAS 41 HARMONISATION AND INITIAL EXPERIENCE

### Introduction

After the IASB issued IAS 41 *Agriculture*, during first quarter 2001, standard setters required to respond to international standards' harmonisation were obliged to meet one final agenda rule-making stage – to incorporate the new standard into local standards suitable for their jurisdiction. There was further work to do since each of the Australian and New Zealand standards were sector neutral for private and public sectors.

In Australia, transfer of IAS 41 involved issue of exposure draft ED 114 on 7 May 2003. There were 20 submissions. Some respondents followed the lead of the AASB who proposed to amend IAS 41 for perceived deficiencies, and even re-litigate what could not be achieved with the IASC. Respondents took the opportunity to lament loss of sovereignty to the IASB, also claiming this involved acceptance of inferior standards.

The new standard, AASB 141 was issued on 22 July 2004 with effect from 1 January 2005.

For New Zealanders, this was the first opportunity to respond locally to IAS 41. ED-90 was issued in April 2002. Prompted by calls for submissions from the local Institute there were a record 197 formal submissions. This number was reduced to 100 by amalgamating individual responses considered to be collusive. A significant number of adverse submissions came from Institute branches, practitioners, farmers and preparers.

It was another two years before the Institute and the Financial Reporting Standards Board (FRSB) prepared a formal report to the Accounting Standards Review Board (ASRB-NZ) recommending issue of NZ IAS 41, effective for reporting periods commencing on or after 1 January 2007, with early adoption permitted. The FRSB recommended the IASB and/or IFRIC be requested to consider the representations made about the impracticality of certain IAS 41 provisions. But nothing further eventuated.



Meanwhile preparers in Australia started changing from AASB 1037 to AASB 141; and in New Zealand to adopting NZ IAS 41. A summary is included to illustrate some of the issues encountered and efforts made to present decision-useful and meaningful financial operational performance presentations for users in interim and annual financial reports.

Many of these issues had featured in local and international submissions so were not unexpected. Independent academics and other commentators also anticipated many of the difficulties and problems likely to be experienced. Possibly these had been discounted by the gatekeepers because of attributed conservatism and preparers' reluctance to change.

Far from the desired ideal agricultural accounting system, some agricultural sectors encountered a '*SGARA Abyss*' and unusual strategies were adopted to mitigate adverse effects.<sup>71</sup> This revealed the lack of dialogue between standard-setter sponsors and preparers and users throughout the evolution of the standard. Preparers and investors doubted whether what was proposed was practical, reliable and decision-useful. In particular, there were doubts whether directors should recognise the resulting financial reports as presenting the conventional true and fair view of the entity's operations and financial reporting without major adjustments – or whether, by mandatory adherence to the standard, there was, by definition, statutory reporting of a true and fair view.

In the event, many listed agricultural entities, users and commentators, in both countries, disagreed with the proposition that IAS 41 met the objective of establishing a high quality standard. It was apparent that by September 2010 the IASB Chairman had reached the same conclusion, as described in [Section 5.5](#) below.

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<sup>71</sup> The writer's Delahunty Trust Research report (2004) was sub-titled "*New Paradigm...or SGARA Abyss*". The former description was used by a leading local academic describing the *Agriculture* standard; the latter was the quote from the CFO of a leading Australian wine company.

## **5.1 IAS 41 Agriculture Convergence in Australia**

The AASB's ED 114 *Request for Comment on IAS 41 Agriculture* (AASB, 2003, May) was the basis to transition locally to adopt IAS 41 for entities (then) currently applying the AASB 1037/AAS 35 *Self-Generating and Regenerating Assets (SGARA)* standards.

The stated purpose of ED 114 was to identify any expected transitional issues for IAS 41 and to identify the extent to which the AASB should converge onto IAS 41 – as AASB 141. A concurrent AASB 1037 post implementation review sought to identify difficulties already experienced when implementing AASB 1037. This is discussed in [Section 6](#).

### **5.1.1 ED 114 Agriculture**

ED 114 was one of a group of five AASB Exposure Draft 'Requests for Comment' on the transition of international standards into formal Australian Standards. They were released on 7 May 2003.<sup>72</sup> Most submissions related to ED 114.

The exposure draft preamble described the new sector-neutral standards for general application by entities with agricultural activities in the for-profit and not-for-profit sectors, for reporting periods beginning on or after 1 January 2005. This conversion date had been confirmed in the *CLERP-9 - Corporate Disclosure* proposals whereby, under Proposal 14, adoption of IASB Standards in Australia would be effective for reporting entities from that date to coincide with the European Union implementation timetable (CLERP-9, 2002).

The AASB intended that IASB standards be the basis for Australian convergence but additional material would be required consistent with Australian requirements. Such scope additions were designed to cover domestic legal or regulatory obligations and any specific public sector issues. These issues and concerns were expanded in greater detail in Ms Ruth Picker's AASB Acting-Chairman's Annual Report for 2002/03 (FRC, 2003, pp. 18-19).

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<sup>72</sup> The others were ED 110 *Cashflow Statements*; ED 111 *Borrowing Costs*; ED 112 *Financial Reporting in Hyper-inflationary Economies*; and ED 113 *Disclosures in the Financial Statements of Banks and Similar Financial Institutions*.

In addition to the full text of the draft proposed standard, the exposure draft provided commentary on:

- A. introductory comparison of IAS 41 with Australian requirements;
- B. technical amendments to conform to Australian requirements; and
- C. proposed additions for the Australian equivalent of IAS 41.

#### **5.1.1.A. ED 114 Introduction and Comparison with AASB 1037**

The differences between the two standards were far from trivial in intent and scope. AASB 1037 addressed SGARAs' recognition, measurement and disclosures and applied to all SGARAs other than those held for non-commercial purposes; that is, it applied to financial accounting and reporting for all non-human living animals and plants that relate to agricultural activity, to non-agricultural activity, and to non-human living assets other than animals and plants.

Under IAS 41 the recognition, measurement and disclosure criteria for agricultural activities were confined to:

the management by an entity of the transformation of biological assets for sale, into agricultural produce, or into additional biological assets (IAS 41:5).

Thus IAS 41 was narrower in biological-asset definitional scope. For example, it excluded animals held for racing; performing circus and theme-park animals; non-human living assets such as viruses and blood cells; and, most topically, investment in heritage forests, zoological specimens and especially forests held as a carbon sink or for supply of carbon credits for sale or own-use. These exclusions were measured at net market value under AASB 1037, but either at cost or fair value under other relevant IAS'.

Another difference related to operating leases for biological assets. These fell within the separate IAS 17 *Leases* standard; whereas, under AASB 1037, the financial recognition and measurement of an operating lease giving exclusive property rights to a lessee over a SGARA was recorded at its fair market value as though the property right itself was a SGARA. Also, IAS 41 accounted for Government grants relating to biological assets as income, when receivable; whereas formerly AASB 1004, not AASB 1037, specified the accounting for grant contributions as an offset against the cost of the SGARA asset.

The fair value measurement basis differed between the two. Under AASB 1037 the presumption was that net market values were always reliably measurable in an active market. IAS 41 made the presumption fair value can be determined for most biological assets. However, because of compromises surrounding its establishment, a cost-rebuttal presumption was permitted where fair value could not be measured reliably on initial recognition, or where market-determined prices or values were not readily available. There was then an ordered fair valuation hierarchy from net present value down to historical cost.

There were also significant disclosure differences. Each standard obliged different disclosures. AASB 1037 required SGARA physical quantities and ownership bases be disclosed for plant/animal categories, and sub-classifications by types of SGARAs within respective categories. However IAS 41 only required physical quantities be identified between bearer- and consumer- biological assets, and whether mature or immature.

#### **5.1.1.B. Technical Amendments to Conform to Australian Requirements**

The AASB proposed the new AASB standard conform to IASB requirements, with two notable exceptions.

The first was for grammatical style. At that time the IASB used a less determinative style of '*should*' (meaning '*ought to*') rather than the AASB's more directive '*shall*' or '*must*'. The AASB proposed to continue using its directive style regardless of the harmonisation objective to adopt IASB standards comprehensively.

The second was the proposed removal of IAS optional treatments in preference to the AASB's preferred standardised accounting treatment without choices.

These indicated the AASB appeared to be litigating for local accounting and reporting practice what it could not achieve by agreement in the international IASC/IASB forum.

A further exception to the word-for-word adoption of IAS 41 was to include, without explanation or justification, some former AASB 1037 disclosures by expanding Australian disclosures for:

Aus 43.1 - separately classifying “plants” and “animals”, and sub-classifications where appropriate, within those classes; and where biological assets are subject to a lease arrangement; and

Aus 49.1 – where biological assets are subject to regulatory or external requirements, which impact on fair value less estimated point-of-sale costs, distinguishing between restricted and total assets, together with the nature and extent of such restrictions.

These exceptions were later removed when AASB 141 was recompiled on 1 November 2007. That recompilation also deleted the Illustrative Examples attached to the standard. Those examples proved to be incomplete and inconsistent, leading to confused interpretations; moreover, they were not formally part of the approved IAS 41 standard.

Apart from these Application and Technical changes, the AASB proposed to adopt IAS 41. It therefore sought comments on transition from AASB 1037 and on IAS 41 adoption.

### **5.1.2 Submissions on ED 114**

Appendix 17 lists the twenty submissions received. Ten confined comments to ED 114. The remainder responded to ED 114 and one or more of the other Exposure Drafts.

Respondents comprised three academics; one listed SGARA public company and two state sector SGARA entities; the Group of 100 and two listed non-SGARA public companies; three public sector Departmental and Auditor-General functions; the ‘Big-4’ accounting firms, two chartered accountants/partners, the Institute of Chartered Accountants of Australia and a private individual, who was the former AASB Chairman.

The commentaries can be divided into general themes on adapting IAS 41 to Australia and on-going specific concerns, still, with the AASB 1037/IAS 41 standards.

There was another category of responses emphasising the AASB’s sector-neutral specifications for public and private sector reporting entities, whereas IFRS were designed solely for private sector ‘for-profit’ reporting entities.

### **5.1.2.A. General Themes Contained in ED 114 Submissions**

In overview, none of the respondents agreed with the proposed amendments to IAS 41 if not a *'verbatim'* or *'word-for-word adoption'* (e.g. Deloitte, 2003; KPMG, 2003; PWC, 2003; Warman, 2003) with the grammatical style amendments being noted as far from trivial (Warman, 2003). There was support in principle for international convergence and IAS 41 transition to Australia; but with important provisos.

There was widespread approval for introducing the proposed rebuttal presumption to cost, not available under AASB 1037. Only Peirson (2003) was opposed to the rebuttal presumption *'since it could lead to identical assets being measured on different bases by different entities'*, but Ernst and Young (2003) noted there were likely to be only *'very limited circumstances [where] fair values cannot reliably be determined'*.

Given its earlier stance, it was no surprise Foster's Ltd. firmly rejected the proposal. Foster's (2003) maintained the valuation bases were too complex and/or misleading for an integrated wine business with unrealised asset valuations affecting reported operating results; the resulting financial statements were not being used for decision-making purposes; and, overall, the costs incurred from meeting these requirements exceeded any benefits, and so were not in the best interests of the Australian economy.

Peirson (2003) also rejected the process of harmonising AASB Standards with IASB Standards as a *'waste of scarce AASB resources [and] difficult to see any net benefit for the vast majority of the AASB's constituents'*.

### **5.1.2.B. Superiority of Australian Standards Setting**

Two academic respondents opposed introduction of IAS 41. They preferred to maintain Australia's claimed better quality standard-setting under AASB 1037. They expressed concern lest Australia adopt weaker quality international standards because these would become legislative instruments under the Corporations Act, 1999 (Langfield-Smith, 2003; Ryan, 2003). Peirson (2003) regretted IAS 41 was narrower in scope; and that entities would be permitted choice of measurement methods on initial recognition.

Ryan (2003) took the sovereignty issue further by deploring the *'virtual handing of authority to set accounting standards in Australia to an unaccountable international standard setting body'*, rather than confining this to a small group in the local accounting profession, who as a result of the transfer of authority, were less able to influence future developments. Thus the AASB would no longer be a standards maker but would become a standards taker to a non-accountable international standards setter.

Langfield-Smith (2003) recommended that before issuing the new standard, the AASB should initiate and undertake further research into basic concepts being measured in the financial statements and also adapt the standards drafting as fit-for-purpose legal instruments, failing which *'any new standard should have a sunset clause of not more than two years'*.

Langfield-Smith also noted *'adopting the approach in IAS 41, rather than AASB 1037, does not overcome my concerns about AASB 1037'* (2003). There appeared to be no cited reference elsewhere about his expressed concerns on AASB 1037; unless Langfield-Smith was the unnamed academic 'User' contributor<sup>73</sup> to the concurrent confidential PIR survey.

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<sup>73</sup> Possibly User U-7; Refer [Section 6.2.2.3](#) below.

### 5.1.2.C. Technical Changes

By far the most consistent plea from respondents was that the IAS 41 standard as then promulgated not be changed on transition to Australia, unless there were really compelling reasons to do so (*e.g.* EY, 2003; G-100, 2003; ICAA, 2003; PWC, 2003).

If changes were considered necessary to improve the standards (ACAG, 2003; Alfredson, 2003; Deloitte, 2003; PWC, 2003; Ryan, 2003) then the AASB should negotiate (*i.e.* lobby) these direct with the IASB and accordingly obtain a revised IAS 41 text. Alternatively, some suggested an addendum translating the IASB style terminology into whatever was required to meet Australian jurisdictional requirements. Deloitte's, for example, drafted a suggested Australian convergence description appendix to the 'pure' IAS 41 standard.

Some submitted the AASB was itself undermining the principle of harmonised standards' convergence by deliberately proposing to establish non-aligned versions and removal of optional IFRS treatments. This would create problems for investors and for any preparers required to report beyond the Australian jurisdiction (BHP, 2003; Woodside, 2003). Moreover, the AASB was inconsistent in its stance on applying IFRS optional treatments. Some were retained on transfer, *e.g.* IAS 7 *Cash Flow Statements*, but not for IAS 23 *Borrowing Costs*. KPMG (2003) urged AASB to '*accept IFRS without amendment and then work with the IASB to improve the quality of IFRS*' – in itself, a telling Auditor observation.

The AASB may already have been aware of the IASB's intentions, or were successful in their private inter-agency lobbying. In 2005, the IASB adopted the AASB's directive style itself when it recompiled IAS 41.



### **5.1.2.D. Specific Comments on ED 114**

In addition to the general comments above, specific comments were:

#### **D.1. Scope**

Some respondents sought to re-litigate the IAS 41 definition of Agriculture maintaining the AASB 1037 definition was more comprehensive and conceptually superior. Regardless of convergence, exceptions should still occur, *e.g.* for heritage SGARAs; zoological specimens, primarily held in the public sector (Deloitte, 2003).

The Auditors-General (ACAG, 2003) noted that the convergence process from AASB standards to sector-neutral IFRS standards needed to integrate Urgent Issue Group (UIG) Abstracts, including for the public sector.

#### **D.2. Errors in IAS 41**

Consistent with other representations for corrections made direct to the IASB, respondents highlighted ambiguity and error where a discounting valuation process is used, with specific reference to IAS 41:21

the objective of a calculation of the present value of expected net cash flows is to determine the fair value of a biological asset in its present location and condition. An enterprise considers this in determining an appropriate discount to be used and in estimating expected net cash flows. The present condition of a biological asset excludes any increases in value from additional biological transformation and future activities of the enterprise such as those related to enhancing the future biological transformation, harvesting and selling. [N.B. Emphasis added]

*Biological transformation* was the standard's distinguishing feature. Where fair value measurement in '*its present location and condition*' was based upon discounted future yields, the specific requirement not to incorporate increases in asset value from future biological transformation, from growth or by silvicultural management plans was, by definition, contrary to current approved measurement methods (ACAG, 2003; EY, 2003; Forestasmania, 2003; FPC, 2003; QDPI, 2003).<sup>74</sup>

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<sup>74</sup> Resolution of IAS 41:21 was left to an IFRIC determination finally approved by the IASB in May 2008.

Respondents emphasised that the standard contained no guidance as to what should be included for consistency and comparability for measuring future costs, yields, prices and discount rates for fair valuation purposes. They recommended prompt clarification of this matter.

Further representations queried whether revenues from valuation changes should be double-counted as different elements of operating results compared to actual realisations (the former as internal entries, the latter as externally-based values derived from realised ownership and risk transfers) or, alternatively, by netting off within cost of sales (Deloitte, 2003; Foster's, 2003; FPC, 2003). The Illustrative Examples attached to IAS 41 were not sufficiently comprehensive to help resolve this issue.

In any event, '*gains arising from changes in fair values*' should be recorded below *profit from operations* (FPC, 2003). Similarly, disclosures should clearly differentiate between revenue realisations and non-cash revenue wealth accruals (Deloitte, 2003; Forestasmania, 2003; Foster's, 2003; Ryan, 2003) and avoid '*a double counting of these revenues*'. Deloitte (2003) highlighted inconsistent treatments, whereby '*some entities [present] both as revenues, others have netted cost of sales against the fair value adjustment or against the [eventual] sales revenue arising from sale of produce*'.

Various submitters recommended urgent referral to IASB, or IFRIC, on these matters carried over from E65 submissions.

### **D.3. Measurement Criteria**

The Forest Products Commission (FPC) approved the rebuttal presumption in IAS 41 which was not accepted for AASB 1037. However, FPC highlighted the urgent need for guidance on relevant criteria for determining an appropriate discount rate to use for inter-entity consistency and comparability. Alternatives were identified as an internal WACC discount rate or some external risk-based interest rate, and whether this applied as a pre-tax or post-tax discount rate (FPC, 2003).

#### **D.4. Sector Neutral Requirements**

Concerns were expressed on convergence with IASB standards for the public sector given IASB's underlying for-profit nexus, when coupled with a stated AASB intention not necessarily to expose all future IASB standards publicly (HoTARAC, 2003).

Given the need for sector neutral standards, insertions into the local equivalent of IAS 41 for public benefit entities should be separately identified pending anticipated eventual transition to different IFRS-style public sector specific standards (Deloitte, 2003); especially since each sector's needs and motivations were so different they cannot satisfactorily *'be accommodated in a single set of standards'* (Ryan, 2003).

Constructive representations were made to retain the accounting treatment for a number of existing Australian standards, *e.g.* for application and disclosures for finance leases, government grants, and restrictions on title. These were seen as superior and more 'principled' than the IFRS version (Deloitte, 2003; FPC, 2003; HoTARAC, 2003).

#### **D.5. Disclosures**

Some respondents maintained disclosures were onerous and excessive. Biological asset disclosures required explicit reconciliations and estimates for physical sales, purchases, production quantities and component movements. None of these were required for any other industry or industrial activity. Furthermore, concern was expressed that disclosures of market-sensitive commercial information would occur for competitors' benefit, some of whom may not be required to report publicly under Australian Accounting Framework rules (Pitcher, 2003).

Forestry Tasmania sought fewer disclosures and, for users' benefit, *'a clearer picture of operational profit as distinct from changes in valuation'* with better disclosures on regulatory or legislative constraints upon harvesting regimes. However, the Auditors-General commended proposed new disclosures as useful but with AASB 1037 title restriction disclosures retained since these were absent in IAS 41.

### **D.6. Keith Alfredson**

The ED 114 and PIR Survey Requests for Comment were initiated in May 2003. On 31 May, Keith Alfredson retired as Chairman of both the AASB and the UIG.

His submission on 27 June, by then in his private capacity, is of considerable interest particularly as his public views now diverged from the established AASB stance on general applicability of the *SGARA/Agriculture* standards. His response, as a former insider ‘gatekeeper’, provides an indication of the probable scope of the internal debate within the AASB, and also the effects of previous external lobbying.

Alfredson (2003) supported IAS 41 adoption, especially the provision that entities were allowed to *‘rebut the presumption that fair value can be measured reliably for a biological asset’*.

Possibly influenced by Foster’s Ltd. representations, his preference was to *‘exclude’* all long term bearer assets, *e.g.* grape vines and fruit trees, which should be *‘carried at cost or depreciated cost, as appropriate’*. With that exclusion, *‘the rebuttal provision can be removed’*. He highlighted that valuing biological assets as a residual value, after deduction of land and infrastructure assets from the total market value of a vineyard, is unlikely to be reliable. Nor was there a market for any such *‘separated asset’*.

Alfredson recognised the inconsistency involved were the AASB, and the IASB, to discontinue their previously adopted valuation basis for accounting for these bearer assets. Regardless, in his view, this would be justified and given credibility if both organisations were now to recognise that *‘a higher degree of reliable measurement is required under any accounting standard when the resultant [value] increment is to be recognised as operating revenue’*.

Accordingly, Alfredson recommended urgent representation to the IASB, or for determination by IFRIC, so that IAS 41, and the new Australian standard, could be amended prior to the formal 1st January 2005 commencement date.

It is noteworthy to record here that although Alfredson was no longer formally involved, these views featured prominently as recommendations from respondents to the PIR Survey, and were subsequently contained in the AASB's recommendations in their PIR Survey Report transmitted to the IASB Chairman five months later.<sup>75</sup>

### **Concluding Comments on Convergence in Australia**

None of the substantive ED 114 responses were accepted by the IASB for incorporation into IAS 41. Afterwards the style of IASB standards did change, possibly as a result of AASB lobbying.

The referral to correct IAS 41:21 to IFRIC was finally accepted and adopted five years later. Notwithstanding that delay, it was widely accepted practice by preparers and auditors to ignore this clause as being wrong and unworkable.

On 10 May 2005, and in substitution to the previously gazetted registration on 22 July 2004, the AASB formally adopted a revised 'Compiled AASB 141' standard operative for periods commencing on or after 1 January 2005. The revision incorporated the directive style with some added scope references relevant for wider sector-neutrality but removed the Illustrative Examples and the proposed extra AASB 'Aus 43.1 and 49.1' disclosures referred to above.

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<sup>75</sup> *N.B.* Discussed in [Section 6](#). The AASB's transmittal letter is recorded as [Appendix 21](#).

## **5.2 IAS 41 Agriculture Harmonisation in New Zealand**

The transfer of IAS 41 *Agriculture* to New Zealand was fraught with difficulty. The Institute of Chartered Accountants in New Zealand (ICANZ) issued Exposure Draft ED-90 *Agriculture* in April 2002. There were numerous calls for submissions. 197 submissions were received. After consolidation of deemed ‘collusive’ submissions, virtually all of the 100 remaining were opposed to proposed changes to long-standing and generally accepted ‘best practice’ sector guidelines issued by the Institute. In total there were approximately 600 pages of submissions. Much of what was submitted reflected issues identified previously during earlier agenda stages for the respective AASB and IASC standards.

Many pastoral and arable farmers noted there would be little change to existing practice. However the proposed standard would not necessarily apply to them as they could opt out of being reporting entities and/or they fell below differential-reporting thresholds.

However a selected few submissions will be commented upon because of:

- participation in the formal IASC steering committee process, or
- insights into agricultural activities in New Zealand not recorded elsewhere.

Three academic contributions, along with others, will be considered in [Section 5.4](#).

In July 2004, the Financial Reporting Standards Board (FRSB) of ICANZ issued a further exposure draft representing the formal process towards issuing the New Zealand Accounting Standard NZ IAS 41 *Agriculture*. In calling for submissions, the FRSB announced it would also be considering the submissions already received on ED-90 – possibly seeking to discourage further submissions. Nevertheless, 12 submissions were made on the second exposure draft, some with new information.

In November 2004, NZ IAS 41 was issued with an effective date for financial periods commencing on or after 1 January 2007, with early adoption permitted - provided the reporting entity fully complied with the equivalents of all other NZ-IFRS standards. There was only one recorded agricultural entity early-adopter; and then only because Carter Holt Harvey Ltd. had a dual listing on the ASX in Australia.

### 5.2.1 New Zealand Exposure Draft ED-90 Agriculture

ICANZ issued ED-90 in April 2002 as a near verbatim copy of IAS 41 (ICANZ, 2002). The rationale for introducing accounting for agricultural activities was expanded in the ‘Discussion Issues’ section. This included recognition of present agricultural exclusions from existing local Financial Reporting Standards (FRS), the importance of the sector to the economy, the alignment programme with the IASB, IFAC and the AASB, and continuation of the Board’s commitment to international convergence of FRS’.

The aim was *‘to assist users of financial reports by ensuring that such financial reports present information regarding the entity’s activities consistently and in sufficient detail’* (*ibid.*, p. 42).

Apart from minor adjustments to comply with the Framework for Differential Reporting the only omission was government grants. ICANZ disagreed with the IASB treatment within IAS 41 and instead maintained grants should be contained in a general standard.

ICANZ, and in particular its Primary Sector Committee encouraged members to provide submissions (Monopoli, 2002, May). Private groups were set up around the country to contribute submissions collectively or individually.

Ms. Sanel Tomlinson, a technical staff member, advised progress on ED-90 submissions and summary high-level content in the Institute’s Report to the FRSB in November:

ED-90: *Agriculture* was issued in April 2002 with the extended comment period ending 31 August 2002. To date, 197 submissions were received of which ± 114 are “duplicated” submissions. This is a list of main concerns raised by respondents:

- respondents acknowledge the need for a standard and the move to fair value and they generally support the idea of harmonisation, but they did question whether the proposals would provide information that would meet the qualitative characteristics for general purpose financial reports;
- fair value of assets resulting from further processing is more reliably determinable than that of assets in the process of biological transformation;
- practitioners might divert to preparing special purpose reports which would result in a lower quality of reporting in New Zealand;
- compliance with the standard would result in a ± 40 % (or \$1,000) increase in the fee charged for the preparation of annual financial statements;
- could lead to taxation of “paper profits” in the future given the IRD’s policy to align tax and accounting treatments;

- recognition of unrealised gains and losses in the statement of financial performance is misleading – should rather be included in the statement of movements in equity;
- due to the lack of sufficient expert and independent valuers, the reliability of valuations could be questionable;
- differential reporting exemptions are insufficient. All entities qualifying under the differential reporting framework should be exempted from the application of the standard;
- requirements are inconsistent with requirements in other FRSs (*i.e.* FRS-3, PP&E; and FRS-4, Inventories)'
- fluctuations in profit could complicate budgeting and forecasting processes;
- standard should not be adopted until other countries, such as North America, have similar requirements – should only require note disclosure in the meantime;
- the inclusion of any element of profit in the valuation of estate or trusts would place the accountant in a potentially litigious position - there must be certainty that income and capital beneficiaries are treated evenly now and in the future; and
- businesses in agriculture are often less sophisticated and are less likely to have sufficient access to highly knowledgeable people than those involved in other industries.

### **5.2.2 Submissions on ED-90**

Although duplications were noted above, Table 24 provides a summary of the 'official' 100 submissions recorded by the FRSB:

***Table 24. New Zealand – Summary of ED-90 Respondents***

<b>Respondents</b>	<b>Nos.</b>	<b>Comments</b>
Institute: Head Office & Branches	10	
Major Accounting Firms	3	Not Deloitte
Practitioners	34	Includes 5 'duplicates'
Chartered Accountants	5	
Industry Representative Groups Includes a summary of a 500 member survey	10	Omits 101 Growers
Non Bearer – Forestry Companies	5	
- Farming Entities	13	
Bearer-Companies	6	Omits 21 Company CAs
Public Sector – incl. Treasury, Auditor-General	5	
Academics	3	
Valuers	3	
Others	3	
Total	100	

Source: Summary of Respondents, ex FRSB List in [Appendix 18](#).

Most submissions contain similar material to representations already made in Australia and to the IASC, as is evident in the ICANZ summary above. However some submissions warrant special mention not noted elsewhere:



- General: some submissions recommended New Zealand not adopt the standard without further phased customisation to New Zealand conditions. This would allow time for preparers and valuers to ensure greater valuation consistency and reporting reliability. Many noted the error in IAS 41:21 and also recommended correction of the Illustrative Examples before formal adoption;
- Harmonisation: whilst a desirable objective, approved by many, implementation should be deferred until IFRS was more universally adopted, in particular by North American countries with their significant local forestry interests and shareholdings;
- Cost/Benefit Assessments: many noted the greatly increased costs expected for valuations (Carter Holt Harvey Ltd., KPMG, Montana Ltd.), for audit (KPMG), for quarterly reporting (Carter Holt Harvey Ltd.) or interim reporting (NZWC Ltd.); others, e.g. Montana, confirmed two sets of books would be required, one for management decision-making and taxation purposes and another for what was described as NZ-IFRS bi-annual '*special purpose*' reporting at greatly increased compliance cost. KPMG noted many small/medium sized entities had voluntarily opted-in to preparing GPFR accounts for tax and financier users, but were now concerned '*clients would [decide to] "opt out" producing second-class reporting for New Zealand's largest sector*';
- Market and user consequences: fair value fluctuations would cause adverse consequences on EBIT for credit and investor ratings, detrimental to investors;
- Agricultural Land: The Treasury, and others, approved of agricultural land being contained in a single standard, IAS 16, in common with all other land. However some respondents noted that land carrying value could either be valued at cost or revaluation under IAS 16. Any 'historic-cost' valuation for land would distort aggregate balance sheet values compared to the 'fair value' valuation-by-deduction method to determine biological asset values attached to land;
- Consumable-SGARAs: Landcorp Ltd. advised '*what is generally proposed (for its livestock, livestock produce and ancillary forestry operations) generally reflects the Company's practice for many years*'. This assessment subsequently changed;
- Forestry-SGARA valuations: submitters were critical of the spot valuation basis proposed at each reporting date as inimical to business judgement and reporting to users. Unlike for short-term crops, the timing of forest harvest had no precise pre-determined date as maturity approached. Forestry harvest decision-making derived

from sophisticated DCF modelling. This sought to optimise current with expected future prices, and holding and harvesting costs relative to further yield-to-maturity. Much forestry land had no alternative use, or value, so that forest land and phased physical improvements, including tree planting, roads and silviculture management plans were all integrated for optimised forest management yield. All costs were capitalised to forest age-block stands pending harvest;

- Changes in Carrying value: a significant number of submissions disagreed with IAS 41 treatment. Landcorp Ltd. noted, for example, in any year, price changes up or down can overwhelm all other items in the income statement. This risked decision-making becoming focussed inappropriately on a short-term horizon detrimental to the business. Consistent with other standards, price changes should be credited to reserves within equity, as they had no bearing on operational performance. NZWC Ltd. identified the precariousness of continuous disclosure forecasts of annual income estimates given reliance on future uncertain spot prices and foreign exchange rates at a future balance date. Montana Ltd., the largest integrated viticulturalist in New Zealand, explained it was impossible to obtain reliable open market fair values for the quantity of all its varietal produce absorbed into its wineries across the country. There was no conceivable real or active market for all their harvest and assets in all regions if actually offered for sale.

### **5.2.3 Ms. Bronwyn Monopoli**

As with Keith Alfredson's submission, Monopoli's deserves special comment. She was a member of the IASC's *Agriculture* SC from 1995-2000, chair of the Institute's Primary Sector Committee, director of Landcorp Holdings Ltd. and a sole practitioner specialist in rural business accounting and reporting for all agricultural sectors.

Monopoli supported need for the standard and much of its underlying conceptual basis.

Her recommendations and comments were:

- to undertake an interim implementation step to obtain high level support through a working group charged with increasing education about the standard and to remove current antagonism impeding likelihood of successful implementation. Whilst many antagonists were ill-informed, some (criticisms) were well-founded, for example:
  1. inclusion of holding gains/losses in the revenue statement, traditionally capital by nature, and still the case for other assets;
  2. measurement difficulties for bearer-assets attached to land;
  3. interim financial statements; and
  4. non-publicly-accountable differential reporting exclusions;
- most farming clients, particularly for livestock, will see no change, albeit price changes normally are credited to equity – but the balance sheet fair value ‘wealth’ effect is understood;
- there would be little change for publicly accountable entities. For example, Landcorp is accustomed to separating out growth and price elements, but not crediting the latter to income. Measurement is not the difficult task claimed by some;
- the greater issue was the link to reporting financial performance and comprehensive income definition, rather than just reporting on agricultural activities (Monopoli, 2002, Oct.).

This latter recommendation also featured prominently in The Treasury’s submission.

#### **5.2.4 Invitation to Comment (ITC) on Proposed NZ IAS 41**

In 2004 the Institute issued its ITC preparatory to considering adoption of the standard (ICANZ, 2004, March). This contained comparative information and tables about existing local pronouncements which would be superseded by the proposal; namely, TPA-5 (ARSB, 1986), TPA-7 (ARSB, 1988), and Research Bulletin R-117 (Davy, 1987).

The ITC commented on practical difficulties already expressed in ED-90 submissions:

- inability to determine ‘fair value’ and the subjectivity of such values;
- impact of fluctuations in financial performance;
- difficulties of measuring land separately from crops; and
- anticipated compliance costs (ICANZ, 2004, March, p. 3).

Notwithstanding these, *‘the FRSB has reviewed IAS 41 and proposes to adopt all the requirements of IAS 41 for its New Zealand-equivalent, NZ IAS 41, for all reporting entities in New Zealand, whether profit-oriented or public benefit entities’* (p. 5).

Constituents, in particular public benefit entities, were encouraged to comment, but for most there was little point. There had been no responsiveness to their ED-90 submissions

and no further positive outcome was expected from the ITC. Even so, there were 12 further submissions – some making precisely that point when seeking oral presentations.

By September, the Institute reported consultations were progressing between the FRSB and industry representatives to identify constituents' concerns and issues (Sealy-Fisher, 2004, Sept.); although these were already well known, just unaddressed.

The following month the FRSB delivered its report to the ASRB-NZ recommending full adoption of NZ IAS 41 (FRSB, 2004, Oct.). This 66 page report summarised in great detail all submissions made for and against. In each case, it noted concerns, but countered with the reasons given in the IASB's Basis for Conclusions, the staff comments made by the AASB, and the matters referred to IFRIC for clarification. Procedurally, it noted all submissions were received, and then made its decisions to:

- advise the IASB it was working through industry concerns;
- accept the impact of the standard including implementation and compliance costs;
- reject certain matters raised in submissions, or to ask the IASB whether the scope of the standard was still appropriate, *e.g.* for bearer assets; and
- leave implementation issues to entities to work through by themselves, or with advisers.

There was an aside recorded that the AASB made its decision to adopt the requirements of IAS 41 after considering their 'Post Implementation Review' of *Self-Generating and Regenerating Assets*.<sup>76</sup> AASB members had noted to the FRSB:

- many entities do not expect to incur difficulties in implementing the requirements of IAS 41 beyond the difficulties already experienced in applying AASB 1037/AAS 35 requirements;
- many entities believe that they will apply the same valuation techniques and derive the same values as they currently achieve; and
- a number of the entities believed that the scope of the AASB 1037/AAS 35 and IAS 41 standards should be reconsidered to exclude the wine industry and bearer self-generating and regenerating assets.<sup>77</sup>

The ASRB-NZ accepted the recommendation to issue the new standard. It was approved under its legislative mandate in the Financial Reporting Act, 1993 (FRSB, 2004, Nov.).

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<sup>76</sup> The AASB and FRSB had a reciprocal mutual harmonisation and exchange agreement entitling, *inter alia*, each to attend the other's meetings.

<sup>77</sup> This reference confirmed, for the first time, representations on the AASB's PIR undertaken a year earlier.

The ASRB-NZ also approved referral to the IASB. These were discussed by the FRSB in December (Sealy-Fisher, 2005, Feb.). The transmittal letter raised the following issues:

- (i) application of the standard to bearer assets that are integrated with land and the potential inappropriate treatment of goodwill when a bearer asset is valued by determining the value of an orchard, for example, and then deducting the known value of its components;
- (ii) recognition of movements in fair values through profit/loss and the importance of the IASB project on Performance Reporting in addressing this issue; and
- (iii) perceived lack of benefits in relation to the costs likely to be incurred for SMEs to measure biological assets, particularly bearer-assets that are integrated with land, at fair value.

In the New Year a full commentary was supplied to ICANZ members confirming issue of the NZ IAS 41 Agriculture standard and matters to be considered by agricultural entities (Scott, 2005).

### **Concluding Comments**

To all appearances all political processes were followed in New Zealand. However any lobbying was ineffective because local standards setters had no discretion to accommodate substantive submissions except by referral back to the IASB and/or IFRIC. In addition, relatively high differential-reporting thresholds and ability to opt-out from continuing to report under NZ-IFRS meant only a few private sector companies were affected.

They rapidly became fewer. In the mid-1990s there were some 25 listed entities in the private sector. Most were forestry companies; now only one is listed. The others were taken over by North American Forestry Companies or Foundations, or by Japanese or Chinese ventures not required to respond to IAS 41. In the Wine Industry, many companies were taken over by American or Australian interests, or they transferred to a private un-listed market, or were de-listed. There are at present only 15 listed agricultural companies comprising six livestock/dairy/herd improvement ventures, four orchard/crop interests, three wine companies, a fishery company and a Maori forestry trust.

New Zealand has not yet adopted the IASB's *Small and Medium-sized Entity* standard. Unless there are significant changes, there is potential for renewed controversy from a powerful lobbying sector whenever adoption is proposed, following the experience with ED-90 in 2002.

### **5.3 Experience with the SGARA/Agriculture Standards**

The previous discussion highlighted respondents' representations and concerns to the new standards. It is relevant to determine whether these were justified, exaggerated or without substance by considering reporting experience. In many cases, concerns were justified. Companies resorted to novel reporting methods to demonstrate underlying 'real' operational performance separate from the impacts of 'unrealised' fair values. For some, the limitations of the standard were revealed by greatly increased unrealised volatility, contagion effects and governance risks not faced by other industrial sector entities. Principal assets on which the business relied were not all subject to fair value rules, thereby creating hidden reserves; whilst for others, the extent of past hidden or over-valued reserves was exposed on transition.

#### **5.3.1 Aquaculture**

##### **Atlas Pacific Limited** (Atlas, 2004)

Atlas solved the valuation issue by recording AASB 141 requirements but added '*the value of SGARAs is only recognised when it can be measured reliably*'. A pearl is the product of a SGARA, and can be valued by sales; but the bearer-oyster, as a living SGARA organism, has no market for valuation reference purposes, therefore the directors '*believe the most appropriate market valuation is cost of production*'. Atlas Pacific's auditor concurred.

##### **Sanford Fisheries Limited** (Sanford, 2010)

Sanford's operations cover salmon, green-shell mussel and oyster farming, and deep-sea, pelagic and inshore-fishing. In terms of managing its aquaculture resources and activities, Sanford's major asset is Fishing Quota and Marine Farm Licences (*i.e.* approx. NZ\$ 450mn. *cf.* total assets of NZ\$720mn.). These in-perpetuity, tradeable, valuable fishing grants are intangible assets, recorded at cost, not subject to depreciation or periodic fair value adjustments, unless for impairment, and referred to as 'hidden reserves' by directors. The net fair value of Sanford's NZ IAS 41 defined biological assets totalled NZ\$7.4mn. - only 1% of its total aquaculture, fishery and trawler fishing assets.

### **5.3.2 Livestock**

#### **Newhaven Park Stud Limited** (Newhaven, 2003)

Newhaven managed thoroughbred horse breeding and trading operations. Directors disagreed with AASB 1037. Thoroughbreds raised for sale were required to be valued at net realisable value (NRV), not at cost. The former 'at cost' policy was maintained '*as a change was considered potentially misleading when sales occur on a regular basis with profits brought to account then*'. Unsold weanlings, colts and geldings inventories were carried at NRV. Breeding stallion interests were valued at NRV but thoroughbred mares were now to be carried at cost. The result was an A\$7.5mn write down in breeding bloodstock carrying value for former revalued assets. The write-down was more than offset by a retrospective revaluation of gaming licences held in Newhaven's hotel interests. Newhaven received a clean audit report. Shortly afterwards, the company de-listed. It then no longer needed to comply with GPFR and AASB 1037.

### **5.3.3 Pastoral/Arable/Crop Farming**

#### **Australian Agriculture Company Limited** (AAC, 2009)

AAC has vast grass-fed cattle breeding and trading operations across Queensland and the Northern Territory covering 1% of Australia's land mass. Its cattle numbers vary for seasonal drought or trading conditions by  $\pm 100,000$  head (2009: 507,000; 2008: 590,000). AAC adopted different valuation methods for its four classes of livestock:

- commercial breeding herds were valued at more stable values determined by prices received for large representative breeding cattle sales similar to AAC's herd;
- trading cattle were valued at shorter term spot market prices at and around balance date;
- bull breeding herd was valued by independent valuation; and
- working-horse and goat herds were valued at NMV at balance date.

Unrealised livestock price change fair value gains were A\$34.5mn. (2008: A\$149.4mn.). Revenue on cropping operations was valued at NMV; but crops-in-the-ground were measured at estimated yields and NMV prices, less point of sale costs - but at cost if yields cannot be measured reliably until it is probable that future economic benefits will flow to AAC. Land was measured at directors' fair valuation, without separate value recognition of its pastoral grass as a biological asset.

**Land Corporation Holdings Limited** (Landcorp, 2006)

Landcorp is a state-owned corporation with the largest combined New Zealand grass-fed pastoral sheep, beef, deer and dairy operations, with separate forestry plantations. SGARA assets were valued at approx. NZ\$200mn. with total land holdings at approx. NZ\$1.2bn.

Landcorp had made generally supportive submissions to the AASB's ED 83 and on ED-90. Changed management and more careful consideration of NZ IAS 41 requirements and consequences resulted in publication of critical articles in the Institute's Journal by their new CFO, Richard Perry.

The first highlighted many difficulties. Primarily, bottom-line results bore no relationship to operational management and financial control due to non-cash-related volatility from unrealised forestry and livestock price changes. These altered NZ-GAAP results by as much as NZ\$25mn. reduction in 2003 and NZ\$37.5mn. increase in 2005 (Perry, 2007, April). Accordingly, these were no longer reported as net 'revenue' in the income statement, as the standard required, but in a '*revaluations gains/losses due to price changes*' block as a final bottom-line section before reporting Net Profit before Tax. The block contained price valuation changes for forests, livestock, financial instruments and property revaluations – the latter normally reported within reserves in equity. Growth was measured in forest holdings, lumber and livestock sales at current market values and for changes in livestock numbers due to births, growth, sales and deaths. These were reported as NZ IAS 41 required, *i.e.* within operational management profit.

The directors maintained NZ IAS 41 requirements envisaged 'realised exit' from the business at each balance date which the company had no intention of doing. '*Reported NPAT becomes a meaningless measure of performance...unrelated to the fundamentals of the entity and its primary production business. Landcorp took the view NZ-IFRS is not an appropriate basis for internal financial management and for management reporting*' (*ibid.*, p. 48). It was irrelevant for evaluation of operational results and dividend calculations.

Prior to compiling the 2006 Annual Report, Perry prepared critical accounting policies for Board and Auditor approval. These were lengthy analyses of NZ IAS 41 for:



1. Livestock valuation: it was agreed livestock for slaughter be valued at market prices, since readily available active markets exist. Breeding livestock had no market value at mid-winter balance date. Following lengthy discussion with the Inland Revenue, agreed to use the IRD's country-wide Average Market Values for both tax and reporting values;
2. Forest valuation: forests to be valued by a DCF method at a pre-tax discount rate used for market sales of farm forests, not commercial forests. The basis was the independent *Standpac* forest valuation model which predicts future cashflows on a 3-year market average of historical log prices and a 12% discount rate. This estimates current forest value on estimated harvest timing and yield; but the discount rate must be kept relevant;
3. Valuation of Grass as a Biological Asset: grass is considered as part of land to be accounted at cost under NZ IAS 16. This was zero. The policy discussion was very lengthy and benefited from a Valuer's professional advice. Two alternatives were considered. The first was that grass is a biological asset, but it was not sold, instead it was eaten by another biological asset, livestock, and grass did not itself transform into another biological asset, it was the same growing asset. The alternative was that grass-growing was an agricultural activity, attached to the land, and that transformation of other biological assets were dependent on it; it was treated as an operational input which could not be measured reliably. The valuer confirmed farm valuation models relate to animal carrying capacity with grass and other factors: like, grass type, drainage, fertility, soil structure, *etc.*, all part of the land, incapable and impracticable to value as components. Agreed, that any value of grass on the land would be subjective, unreliable and incapable of confirmation;
4. Grass grown for Hay and Silage: at June balance date grass was dormant. Over the spring/summer months own-grass is converted to silage, baleage and hay but used as farm-feed input for operations and not sold, so agreed they were not recognised as harvested products; more realistically, it was assessed technically as produce, but immaterial;
5. Accounting for Agricultural Produce: previously inventory was carried at 70% of estimated realisation; the standard required fair value at harvest but this could not be cost-justified so Landcorp proposed a fair value best estimate at balance date, less estimated cost-to-sell.<sup>78</sup>

Perry was critical of the IASC's *'one size fits all approach'*. He quoted his CEO, Chris Kelly, as stating *'IFRS is a nightmare'* and Landcorp's alternative reporting was tantamount to saying *'ignore IFRS' – that was ludicrous for a country like New Zealand'*. Perry cited other examples from other companies. His principal conclusions were to:

- provide for comprehensive income statements that include fair value reporting on assets, with a clear delineation between gains or losses from these sources and cash-related (operational) gains and losses; and
- ensure concerns on IAS 41 are highlighted to international accounting setting bodies and lobby for review of IAS 41 (Perry, 2007, April, p. 10).

The second article continued his criticisms: *'NZ IAS 41 can, quite simply, lead to financial reporting that obscures and distorts the fundamental performance of primary sector entities...but the solution is refinement of IAS 41, not abandonment'* (Perry, 2008, May).

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<sup>78</sup> Provided to the writer by Richard Perry.

**PrimeAg Australia Limited** (PrimeAg, 2010a)

PrimeAg undertakes seasonal wheat, chickpea, cotton and sorghum crop operations, supported by extensive Water Entitlements integrated with its seasonal cropping activities. Its rural properties also carry livestock. At balance date, crops in the ground are valued at fair value, less costs to sell, with fair value determined on an estimated yield at the commodity spot price. If the crop is immature, defined as too early to predict yield reliably, it is carried at cost until '*it is probable that future economic benefits will be received*'. Crops and cattle assets were recorded at A\$6.3mn., with net operating profit at approx. A\$31mn. PrimeAg's principal asset is intangible Water Rights at A\$89mn. held for risk management, irrigation and biological viability. They are tradeable rights, legally separable from land and recognised at cost, less impairments, as the deemed 'fair value'.

A notable feature of PrimeAg's financial statements and forecasts is the significant variability caused in crop yield from seasonal rainfall, temperature and water rights availability, and in domestic and export crop prices caused by A\$-volatility. Directors provide periodic ASX continuous disclosure net income forecasts for a base case, high/low cases and  $\pm 20\%$  price and yield ranges. The 3 November 2010 base case, *2011 fair value net operating income* forecast was A\$16.3mn. in a range of \$23.7mn. to \$8.9mn.; and the  $\pm 20\%$  range was from \$38.9mn. to minus \$2.6mn. These fair value disclosures were so wide as to be of doubtful relevance for users, except as a measure of volatility (PrimeAg, 2010b).

**5.3.4 Wine Companies****Southcorp Limited** (Southcorp, 2000-2003)

Southcorp's pre-SGARA vineyard valuation practice in 2000 was to capitalise all individual vineyard development costs, including interest and overhead costs, for the initial four years. After this, vineyards were considered to be in commercial production. Depreciation was then on a straight-line basis over their expected useful lives, varying between 15-30 years.

On adoption of AASB 1037, on 1 July 2001, directors determined comparative values as at 1 July 2000. Vines within vineyards were transferred to 'grape vines'. These were measured at net market value (NMV), with period value-changes recognised as revenue or expense in the income statement. Measurement was by directors' valuation being the

difference between the NPV of forecasted cashflows, based upon expected market price, value and quality of grapes generated by vine blocks and an independent valuation of NMV of other integral vineyard assets. Formerly, costs of harvested grapes were capitalised to inventory but now were recognised as revenue at NMV and vineyard costs as expenses.

**Table 25. Southcorp Limited - Key SGARA Results 2001-2003**

YEAR		2001	2002	2002	2003
Period		Annual	Half	Annual	Annual
Grape Vines Fair Value	A\$ mn.	167.7	204.2	172.6	170.5
Owned/Leased Hectares		7,720		7,720	8,039
Net increment Vines NMV	A\$ mn.	-5.0		+0.9	-9.0
NMV Own grapes sold	A\$ mn.	83.0		63.4	57.4
NMV Own-grapes in Cost of Goods sold	A\$ mn.			-11.0	-15.7
Net SGARA profit/loss before tax	A\$ mn.			0.2	-22.4

Source: Southcorp Limited Annual Reports 2000-2003.

- Southcorp's vineyards were located in Australia, France and the United States. The half year report recorded value of the growing crop in Australia and the dormant harvested vines in the northern hemisphere; and *vice versa* at the 30 June full year. Inter-entity comparisons were virtually impossible. For interim reporting, Southcorp assessed a deemed internal value for the expected harvested crop capitalised into the Vines value;
- NMV of own grapes included NMV of harvested grapes and full harvesting costs;
- harvested grapes were recorded in inventories at harvest at NMV with that net realisable value adjusted annually for the original harvested grapes still maturing within inventory and with separately assessed estimates of selling, marketing and distribution costs attributable to that original maturing grape juice;
- cost-of-sales release to income therefore occurred to adjust prior years' NMV held as cost-of-inventory since it took many years post-harvest for final sales realisation;
- the net SGARA profit/loss before tax was the net result after the above adjustments and deduction for other vineyard operating costs. The annual result therefore included deemed net revenues, actual operating costs, adjustments for prior periods, and inventory impairments - if current NMVs were less than previous NMVs;
- declining NMVs in 2003 therefore had adverse 'contagion' impacts on changes in both the current vine asset and harvested produce values, and for grape juice held in inventories. The opposite applied in periods of rising prices, such as in 2002.

**Foster's Group Limited** (Foster's, 2001-2003).

In contrast to Southcorp, and to its chagrin, Foster's decided to adopt AASB 1037 early, with effect from 30 June 2001, to take advantage of rising grape prices compared with 2000 and while Foster's was in an aggressive growth phase. The contribution from the unrealised NMV Vines component in 'Net SGARA profit/loss' is evident in Table 26:

**Table 26. Foster's Group Limited – Key SGARA Results 2000-2003**

YEAR		2000	2001	2002	2003
Period		Annual	Annual	Annual	Annual
Agricultural Assets	A\$ mn.	80.2	366.7	357.7	328.5
Owned/Leased Hectares		3,300	7,600	7,800	7,600
Net increment Vines NMV	A\$ mn.	nil	+ 71.6	+ 124.2	+ 51.3
Net SGARA profit/loss before tax	A\$ mn.		25.7	44.2	-14.3

Source: Foster's Group Limited Annual Reports 2001-2002

Like Southcorp, Foster's owned or leased vineyards in each hemisphere throughout the major wine growing regions in Australia, U.S.A., Italy and New Zealand. Foster's also owned olive groves in Italy and New Zealand, but these were insignificant at <0.5% of vineyard values.

- in June 2000 and 2001 directors obtained independent vineyard valuations. Directors then determined component land and vine values with the latter derived by deduction as the NPV of forecasted cashflows expected to be generated from the vines. Subsequently, directors made internal annual assumptions about expected vintage growth, yield, quality and prices at balance date;
- in accordance with AASB 1037, agricultural asset values were determined annually with any change in market value recognised in the current period; costs incurred in maintaining assets were recognised as expenses, as incurred, and the net market value of picked grapes and olives were recognised as revenue;
- inventories of wine stocks, recorded as work in progress at cost, represented net market values for the current and prior years. In 2003 there was an element of amortisation of the prior period grape valuation increments;
- there were two features of Foster's financial statements compared to Southcorp:
  - the paucity of disclosures with bare minimum detail; and
  - the inclusion in Foster's overall results of a summary *EBITDAS* line – being 'Earnings before Interest, Taxation, Amortisation and SGARA', a line for the 'SGARA' result, being the final line in Table 26, to obtain the 'EBITDA' Group result.
  - Foster's claimed in a letter to AASB Chairman, Keith Alfredson, on 23 August 2002, reproduced in [Appendix 19](#), p. 95:
 

consistent with the financial results announcements of other major Australian companies in the wine industry, Foster's now presents its financial results to the investment analysts

excluding the effects of SGARA. It has taken a number of years for analysts to understand the unique SGARA accounting requirements, which has resulted in constant questioning of Foster's senior management to explain the impact on the financial results. To assist their understanding of the financial impact, Foster's releases the forecasted future year financial impact of SGARA. The analysts seek to reverse the SGARA EBITA (*sic*) impact from inventory, thereby reverting inventory back to historical cost.

**BRL Hardy Limited** (BRL-Hardy, 1999-2001)

Unlike the other major wine companies, BRLH balance date was on 31 December, not 30 June. It had vineyards in the principal wine producing regions in Australia, France and New Zealand, but mostly in Australia.

**Table 27. BRL Hardy Limited – Key SGARA Results – 2000-2001**

YEAR		2000	2001	2002 Note 1
	Period	Annual	Annual	Annual
Agricultural Assets	A\$ 000	33,321	38,811	43,676
Owned/Leased Hectares		2,068	2,148	2,318
Transfer Vines from PP&E	A\$ 000	20,320	NA	NA
Initial Restatement of vines on adoption of SGARA accounting	A\$ 000	11,190	NA	NA
Net increment Vines NMV	A\$ 000	1,811	1,835	3,288 )
Change in NMV grapes on vines	A\$ 000	1,229	2,073	)

Source: BRL Hardy Limited Annual Reports 1999-2001.

- in 1999, prior to adoption of SGARA accounting in 2000, vineyards were revalued triennially, based on fair market value for existing use. Revaluation increments were credited to reserves within equity without any deferred capital gains tax charge - unless there was an intention to sell the assets concerned. Development costs for new vineyards, including materials, labour, overhead and borrowing costs were capitalised to capital work-in-progress. Capitalisation continued after planting to commercial maturity, normally three years. Depreciation was 20-50 years based upon estimated useful lives of vine improvements;
- on adoption of SGARA accounting for year ended December 2000, the change in accounting policy lead to an increase in operating profit after tax of A\$2.0mn. BRLH took the opportunity on adoption to elect the option under AASB 1041 *Revaluation of Non-Current Assets* to revert 'Vineyard Improvements' to a cost base from 'Plant and Equipment' on first application of the standard so as to 'unlock' revaluation reserves. Other accounting measurement procedures were as reported by Southcorp and Foster's;
- since BRLH balanced at calendar year-end, the bottom line in Table 27 recorded the incremental asset value for the assessed maturing grapes on BRLH's local vines;

- after the take-over by Constellation Brands in the U.S.A. on 27 March 2003, BRLH de-listed from the ASX. The company filed a final ASX audited Accounts disclosure for 2002. On adoption of parent company US-GAAP accounting policies, the CFO advised the writer the ‘SGARA Abyss’ had ended; all vineyard values reverted to cost. Quarterly reporting was now much easier to prepare, and more meaningful.

**Pipers Brook Vineyard Limited** (Pipers-Brook, 2001-2002)

This small Tasmanian wine company is included because of the decision made by management to embed SGARA principles by recording all their vineyard operations on an NMV basis. This required restatement of previous vineyard records as advised by their CFO during the writer’s Delahunty field research (Milne, 2004). Tax return information was held and prepared outside these records for special purpose financial reporting.

For the 2001 year, adoption of AASB 1037 resulted in increased revenues of A\$3.9mn, increased expenses of A\$2.6mn. and an increased vineyard operating net profit of A\$ 1.1mn. This included an unrealised \$0.7mn. vine value increment and a \$0.3mn. inventory write-down. In 2002, the vineyard operating loss was reported at A\$0.7mn. after including A\$0.4mn. unrealised ‘gross increment in NMV of vines’. The loss was attributed to an unusually low-yielding vintage, resulting in an approx. 50% NMV reduction in NMV of grapes harvested below the 5 year rolling annual average.

Pipers Brook was subject to a takeover by its Belgian parent, Kreglinger, in March 2002 and subsequently de-listed.

**New Zealand Wine Company Limited** (NZWC)

As early as its 2000 Annual Report, the directors noted progress on the new SGARA accounting standard in Australia.<sup>79</sup>

Initial consideration was given to early-adopting the AASB 1037 standard, by reference, to recognise in the income statement changes in NMV for SGARA assets. In the 2001 Report, directors were more reticent, not wishing to overstate profits as was observed in Australia. In their 2002 Report, directors stated *'we are not happy with the SGARA standard...(nor) with the ED-90 proposals either...all we seek is not to overstate profits in any way and to adhere to the "true and fair view" convention'* (NZWC, 2002). In the meantime, during the first three years after planting and until commercial maturity, traditional capitalisation of vineyard establishment costs continued for, with valuer's annual aggregate vineyard net revaluations credited to reserves within equity.

The first year of application of NZ-IFRS was for financial year beginning 1 July 2007, the last adoption date possible. The 2007/08 Interim Report to 31 December 2007 was the initial NZ-IFRS report. This required restated comparatives for the previous 31 December 2006 interim period and restated full 30 June 2007 financials.

Directors proposed a matrix income presentation for the Interim 2007/08 period to disaggregate commingled traditional cost-based performance/realisation elements from unrealised vineyard valuations and unrealised inventory profits pending eventual third party sale. The presentation was based upon an early draft of the 'matrix project' report commissioned by the IASB (Tarca *et al.*, 2008). In 2005 the IASB contracted Australasian academics to study a matrix-reporting project. In turn, this project had arisen out of an earlier joint project between the IASB and ASB on the 'performance reporting project'.

The reported matrix-project objective was to *'categorise and display all income and expenses for a period in a way that enhances users' understanding of the entity's financial results'*, and to support contemporary work with the FASB. This involved reporting comprehensive income as a single statement, with line-by-line disaggregation of income statement items between re-measurements and before re-measurements, taking items

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<sup>79</sup> The writer was a director of the NZWC, and its predecessor, Grove Mill Wine Co. Ltd., from 1997-2008.

directly to equity and permitting ‘cycling’ (*ibid.*, p. 185). Preliminary matrix-presentation findings were reported as positive for enhanced usefulness and decision-making; but further study was required from real-world users to ensure better outcomes were achievable, especially to help determine the investment community’s risk, forecasting and valuation requirements (p. 211).

Directors proposed that the third, outside, column represented full mandatory IFRS-reporting, the middle column recorded all unrealised book and closing valuation entries for IAS 39 *Financial Instruments* and IAS 41 *Agriculture*, and the first, inside, column all realised transactions. Deloitte, as Auditor, objected advising the full year Accounts were likely to be qualified because: this was pioneering and sophisticated pro-forma reporting; NZ IFRS 1, for first time adoption, did not envisage a columnar income statement presentation; and, finally, the first column although presented as ‘underlying operational performance’ was equivalent to ‘cost-based’ practice, inimical to NZ-IFRS principles.

However there were two matrix-presentation precedents already reported in the U.K. and one in Belgium by companies with Palm Oil and Rubber interests in Indonesia and Malaysia.<sup>80</sup> M.P. Evans plc was audited by Deloitte International and had adopted matrix-income reporting. Accordingly, Deloitte N.Z. agreed to a matrix presentation for the income statement and balance sheet - but only in respect of NZ IAS 41 for strict comparability with their international precedent.

However, unlike these overseas companies with a US\$ functional currency, and therefore with limited IAS 39 application, significant quantities of NZWC’s exports were denominated in foreign currencies with unrealised hedged and unhedged forward-cover commitments. Deloitte N.Z. required these unrealised forex hedging items to be reported in the inside column as operational matters separated from their IAS 41 reporting precedent.

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<sup>80</sup> In the 2007 Financial Statements for: *SA Sipef NV* – for palm oil and rubber, tea and tropical fruits and plants; *M.P. Evans Group plc* – for palm oil, rubber plantations and for beef operations in Australia; and *Anglo-Eastern Plantations plc* – for palm oil and rubber.



The Interim 2007/08 presentation was a first in New Zealand. The Note explanations were comprehensive for first-time IFRS reporting requirements, with new explanations for unrealised NZ IAS 41 requirements, and the rationale for the matrix-reporting content.

**Table 28. NZ Wine Company Limited – 2007 & 2008 Interim Unaudited Results**

INTERIM Income Statement: @ 31 <sup>st</sup> Dec.	2008	2008	2008	2007	2007	2007
Unit NZ\$ 000s	Excl. IAS41	IAS 41	Full IFRS	Excl. IAS41	IAS 41	Full IFRS
Revenue	6,213	-	6,213	5,601		5,601
Vines Gain/Loss		+1,468	+1,468		+923	+923
Harvested Grapes	-	-	-			
Vineyard Expenses		-1,468	-1,468		-923	-923
Cost-of-Sales & Prior years NMV Adj.	-4,072	-52	-4,124	-3,339	+25	-3,314
Profit before Tax	1,055	-52	1,003	1,511	25	1,536

Source: NZWC Ltd. Income Statement for Six Months Ended 31 December 2008 (NZWC, 2009, March).

For interim reporting, all Vineyard Expenses were capitalised at cost to the Vines, being immature with no market. The IAS 41 cost-of-sales column 2 figure recognised the realised/unrealised holding inventory gains/losses from NMVs for earlier years' harvests.

However the Annual Financial Statements reveal the full IAS 41 effects, post harvest.

**Table 29. NZ Wine Company Limited – 2007 & 2008 Annual Matrix Results**

ANNUAL Income Statement - 30 <sup>th</sup> June	2008	2008	2008	2007	2007	2007
Unit NZ\$ 000s	Excl. IAS41	IAS 41	Full IFRS	Excl. IAS41	IAS 41	Full IFRS
Revenue	11,996	-	11,996	11,309		11,309
Vines NMV Gain/Loss		+280	+1,468		+561	+923
Harvested Grapes	1,613	585	2,198	1,429	-199	1,230
Vineyard Expenses	-1,613	-	-1,613	-1,429	-	-1,429
Cost-of-Sales & Prior years NMV Adj.	-7,659	125	-7,534	-6,745	-203	-6,948
Net Profit before Tax	2,008	990	2,998	1,346	149	1,495

Source: NZWC Ltd. Income Statement Report for Year Ended 30 June 2008 (NZWC, 2008).

Illustrative of the extent unrealised components could 'distort' actual and operational performance on a full IFRS-basis, the reported 2008 column 3 Net Profit before Tax increase was 100% over 2007, but the Column 1 operational figure increased by 50%, excluding IAS 41 fair value effects. The Column 2 IAS 41 impact was an increase of 564%, of which 146% was a combination of unrealised- and prior year realised-inventory losses/gains in actual wine sales.

In 2009 and 2010, the NZWC adopted the ‘single column’ Landcorp income statement reporting procedure encouraged by Deloitte, auditors to each. In 2010 the NZ\$ appreciated faster than hedge cover. This was coupled with record harvests and grape over-supply, causing falling grape prices and impaired vine values. Taken together, these resulted in greater volatility between realised operational and financial performance vs. IFRS-based NPAT performance. Balance sheet asset values were also adversely impaired by the effects of a decline in vineyard land revaluation adjustments in reserves, especially in 2010, because of distress vineyard sales from lower regional grape prices.

***Table 30. NZ Wine Company Limited – Recast Annual Audited Results 2007-2010***

ANNUAL Income Statement @ 30 <sup>th</sup> June	2010	2009	2008	2007
Unit NZ\$ 000s	NZ-IFRS	NZ-IFRS	NZ-IFRS	NZ-IFRS
<b>Underlying NPBT</b> excl. NMV revaluations & Unrealised IAS 39 Fx cover Mark-to-market	-46	571	1,895	1,246
Unrealised IAS 39 Fx Cover Mark-to-Market	-396	+2,580	+113	-
Unrealised Vines values gain/loss	-1,383	-726	+280	+551
Unrealised harvested Grapes gain/loss	-306	-366	+585	-199
Realised harvest Grapes prior NMV gain/loss	96	-216	+125	-203
<b>Full NZ-IFRS Net Profit before Tax</b>	<b>-2,035</b>	<b>1,843</b>	<b>2,998</b>	<b>1,495</b>
<b>Reserves – Land/PPE revaluation changes</b>	-1,251	-14	+462	+392

Source: NZWC Ltd. Annual Reports - (NZWC, 2008, 2010).

The presentation identified the operational, realised ‘Underlying Net Profit before Tax’ and the individual unrealised IAS 41 and IAS 39 component elements required to be reported in the income statement to obtain the full NZ-IFRS ‘Net Profit before Tax’. This highlighted how far the extent of unrealised fair value asset and produce carrying value changes, and inclusion of harvest fair value in inventory, can mask underlying cash/accrual performance. This increased the volatility and precariousness of ‘bottom-line’ NZ-IFRS reported results for 2009-10 for directors’ dividend determination purposes.

### **5.3.5 Forestry Entities**

In Australia forestry accounting was an original principal purpose for and beneficiary of the SGARA standard whereby, *inter alia*, forest growth, and later on, values were credited to the income statement. As noted earlier, North Limited was the only entity worldwide to make submissions on all stages of standard development to the AARF/AASB and the

IASC.<sup>81</sup> North Ltd. was originally a subsidiary of North Broken Hill Peko Limited, variously trading as North Forest Products Limited and then North Group – until taken over by the Rio Tinto Group in August 2000, at which time it was de-listed. On 29<sup>th</sup> May 2001, North Ltd. was bought by Gunns Limited.

### North Limited/Gunns Limited

All of the North Ltd. submissions were consistent over the years:

- there should be a standard for Agriculture, but the standard should differentiate between short term cropping vs. long-term regenerative activities – like forestry;
- biological transformation should only be recorded annually; and recognition valuation should reflect that no efficient, active or liquid market exists for a forest until product is close to harvest or actually harvested at maturity – therefore a fair value surrogate should be permissible, such as NPV;
- although North could split changes in carrying value between growth and value, they did not support growth to be credited to the income statement and price effects credited to reserves; instead, both should be carried within equity reserves until harvest realisation. This was consistent with other assets. The reasons provided were disagreement on recording unreliable, unrealised profits or losses in the income statement, with the subjectivity involved, and implications for determination of dividend availability for distributions. North recommended consideration be given to a generalised and consistent performance measurement approach to recording and treatment of all unrecognised gains and losses;
- North disagreed with land being separated and treated differently to the integrated forest asset. It recommended imputing a land rental to the forestry valuation model;
- at harvest, inventory should be carried at cost pending clarification of taxation consequences;
- North provided detail of its accounting treatment for changes in carrying values within its ‘Regenerative Resource Revaluation Reserve’ (North, 1996); finally
- North offered IASC staff the opportunity to ‘field test’ the IASC’s E65 proposals.

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<sup>81</sup> B.M. Macdermott of North Forest Products was an original AARF Advisory Panellist to consider DP 23.

Gunns Ltd. reflected AASB 1037 requirements, (Gunns, 2004), prior to adoption of AASB 141 in 2006:

- Gunns adopted similar accounting policies for both its forestry and grape vine interests when separating land values from the NPVs for respective SGARAs. The nominal discount rates adopted were 10% for forests and 12% for vines. For forests, under AASB 1037, the directors' valuation basis was at cumulative costs of establishment until the NPV of future cashflows exceeded cumulative establishment cost. Gunns adopted internal assumptions about future growth, costs, existing silvicultural and harvesting practice coupled with estimated yields per hectare and for expected year-of-harvest for timber on-sale to Gunns' integrated pulp mills. For their vineyards, Gunns assessed expected market prices, yields and qualities of grapes with post-harvest grape price based upon third-party arms-length realisations;
- post-IFRS, under AASB 141, Gunns supplied an initial A-GAAP reconciliation between the two standards (Gunns, 2006). Whilst the discount rate remained WACC-based, further adjustments were required. The previous 'nominal' rate was replaced by the equivalent 'real' discount rate. Therefore, on transition, opening retained profits were reduced by A\$23.8mn. for the consolidated entity with a balance sheet offset for deferred tax liability of A\$7.14mn.;
- under AASB 1037, the revaluation calculation was based upon net harvest value, whereas under AASB 141 the gross increment was disclosed as Other Income and the harvest value as Raw Materials and Consumables Used. The net effect was to record a net loss before tax of approx. A\$9.8mn. on transition at 30 June 2005;
- apart from transitional reporting, Gunns' disclosures were the barest minimum. There were disclosures for Current and Non-Current Biological Assets for Standing Timber and Horticultural Assets respectively, together with quantitative disclosures for incremental annual timber volume yield and actual timber volumes harvested; and vineyard hectares and fruit volumes harvested.

**PricewaterhouseCoopers Surveys of World-wide IAS 41 Forestry Accounting.**

In 2009 PWC published a study, described as the first of its kind, into the major changes in ‘standing timber’ accounting practice worldwide following adoption of IAS 41 (PWC, 2009). The purpose was to determine for increasing numbers of preparers and user investors how ‘fair value’ was being applied and what key judgements were being made by forest entity preparers. PWC was careful not to pass judgement on the standard but rather to identify problems with emerging current practice. This was complemented by an update two years later (PWC, 2011). The new study confirmed earlier findings that inter-entity comparability was complicated, or could not be achieved, under IAS 41, and the standard was not applicable to long-growth forests. However, improvements were possible - with more comprehensive disclosures.

The 2009 study was based on the 2007 financial statements for 19 entities across 5 Regions and the 2011 study upon the 2009/10 statements for 25 entities across 6 Regions. Some from the 2009 study no longer reported so were replaced by new-adopters. None were included for Brazil, Canada or the U.S.A. since IAS 41 was not yet adopted there.

The key critical findings on judgement areas in both reports were:

- reliable market-based standing timber prices are rare. Even where market prices are available these must be imputed by deduction from the integrated land and timber asset as a result of DCF-based computer modelling. This was the most common method of determining fair value;
- the significant modelling assumptions adopted were the discount rate, future or current timber prices, forestry costs, silvicultural practices and growth rates, harvest plans and associated nominal or real inflation rates;
- the majority of preparers appeared to have concluded that transparent market price discovery is the exception not the rule, therefore NPV is used as an NMV-surrogate with multiple supporting valuation parameters, including historic cost pending maturity and satisfactorily reliable fair value bases. Reliable market price-based valuations were evident for short-rotation timber crops when they are classified as mature; but, for longer rotations, preparers use valuation techniques and judgements, *e.g.* price adjustments typically smoothed to remove short-term volatility, contrary to

IAS 41. An example given was use of 12-quarter rolling historical average prices with extrapolations for inflation, timber price, and cost assumptions;

- the discount rate used was the most commonly reported parameter, but only from about two-thirds of surveyed entities. Rates ranged from pre-tax 5.5% to 13.5% nominal; Gunns' Ltd. used 9% real, and a Nordic company applied 5.5% to 6.25% real. There was no common pattern. Rates varied regionally and for regions within a company's operations, reflecting risk and site-specific geographical factors;
- a principal PWC recommendation was to enhance disclosures. Modelling assumptions on key valuation parameters were not always provided for company-specific judgements, for their species rotation and management harvest plans - including future assumptions for growth yields, log prices and pricing criteria, harvest and other silvicultural costs and, importantly, discount rates used;
- PWC also noted that only three companies provided sensitivities on the effects on asset values of changes in one or more of prices, volumes, costs, growth and discount rates. None discussed effects of alternative-use valuations or other valuation perspectives, *e.g.* for effects of carbon sinks on forest values.

Thus, because of the importance of valuation assumptions on reported profits, PWC encouraged greater disclosures and transparency about critical assumptions. However, PWC was cautious not to be critical of IAS 41. Their findings are reminiscent of the variability of pre-SGARA forestry accounting practice in Australasia a decade earlier. The objective of resolving the forestry reporting issue to ensure enhanced comparability between reporting entities under IAS 41 appeared not to have succeeded.

### **Concluding Comments on experience with the SGARA/Agriculture Standards**

Many of the difficulties and issues arising from experience can be attributed to inadequate design in the standards between consumable- and bearer-SGARAs and the difficulties arising from lack of distinction between 'realised' and 'unrealised' revenues recorded in the income statement, and not recorded in reserves, pending realisation. There was a lack of 'learning' from recommendations made to improve respective standards. Instead the *inside access* model was evident, sponsored by key insiders to meet other objectives.

#### **5.4 Academic Articles and Submissions on the Agriculture Standards**

There was a history of articles and submissions by academics around the world prior to, throughout and after the various rule-making stages for the *Agriculture* standards. These should have alerted Board members, and in particular key insider technical staff, that the proposed Australian and International standards were likely to cause difficulties, especially for bearer-SGARA entities. There were questions as to how sound the proposed standards were relative to measurement principles in the conceptual framework. Some provided studies as to how existing practice would change, sometimes materially for certain sectors. The surprising result was how little academic advice appeared to be heeded. Evidence of the standards-setter archetypes described by Mitnick (1980), the prevalence of the *inside access* model (Cobb *et al.*, 1976) and lack of expected experiential learning by policy makers (Sabatier, 1977).

Initially, the prognosis for the new standard was positive with '*a strong conceptual framework but might need further instruments for its implementation in practice, given the limitations of the agricultural sector*' (Argilés and Slof, 2001). The instruments related to the cash-based European Farm Accountancy Data Network as a useful recognition model, in conjunction with the IASC's accrual basis, but it was noted difficulties might arise from practical application within the European regulatory system.

Charles Elad (2004) disagreed. He claimed IAS 41 was incompatible with the European Fourth Directive. This might have accounted for aspects of the EU (2000) submission on E65 - but also with the French *Plan Comptable Général Agricole* for French farmers and in undeveloped and newly-industrialising Francophone countries. The latter were amongst the expected beneficiaries of the World Bank's original IASC agriculture project grant.

Elad postulated that the IASC wanted to push the fair value '*reforms in order to establish a precedent on fair value accounting and recognition of unrealised income*' (2004, p. 632). Camfferman and Zeff had made similar observations (2007, pp. 402-3)

Based upon his study of DSOP and E65 submissions, Elad (2004) adduced a number of reasons why the alleged merits of IAS 41 were debatable. Amongst these were:

- the DSOP comments by Colin Saunderson (1997), as an experienced practitioner in under-developed countries. Similar comments were noted by Professor Hajimi Arai (Arai, 2000) that such radical departure from historic cost accounting would be unlikely to be acceptable in Japan in the near future;
- the presumption that fair value can be determined reliably. This can be rebutted where fair values, or estimates, cannot be determined with reliability – however not for the reasonable situation that costs of determining fair values were unreasonably excessive;
- surrogates impaired inter-entity comparability where market prices were used from non-comparable bases for similar products in other markets, or for assets determined by NPVs with inconsistent assumptions;
- the standard envisages annual revaluations, which might be onerous or expensive, particularly in developing countries, where expert valuer resources were limited;<sup>82</sup>
- adoption of IAS 41 in developing countries by forest exploitation companies operating extraction regimes under logging concessions. These finance leases under IAS 17 *Leases* were required to be measured and applied as biological assets under IAS 41. Changes in fair values were treated as revenue, but in those countries fair value determination was near impossible quite apart from the '*stratospheric phantom profits*' on existing logging concessions from unrealised holding gains on initial recognition. Doubts were expressed whether IAS 41 should be applicable at all to these forestry management regimes.

There were two other general observations. Elad referred to one potential benefit for developing countries offering timber concessions, namely '*the shift from historic cost to fair value accounting might strengthen the capacity of host governments in less developed countries to impose tax policies based on market value income which generate more revenue...thereby helping to reduce the potential for expropriation of natural resources*' (2004, p. 632).

Elad had also enquired about the IASC Field Test as a follow-up to E65 submissions by Southcorp Ltd. and The Group of 100 (IASC, 1998). Staff advised it had been a '*postal questionnaire survey rather than on actual observation of the implementation process in an organisational setting*' as Southcorp, and others, had offered (Elad, 2004, p. 635).

Overall, Elad concluded IAS 41 '*appears to have portrayed a dubious triumph of theory over pragmatism*' (p. 638).

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<sup>82</sup> The standard requires revaluations at every reporting date; that is, for Interim reporting too.



Common themes emerged from academic submissions on the DSOP and the various ED 83, E65 and ED-90 exposure drafts:

- resistance to separate measurement bases in standards for different industries and types of tangible or intangible assets (Ryan, 1997; Amen, 2000; Clark *et al.*, 2002); high degree of unanimity on NMVs for all assets and liabilities, or all at cost. If NMVs were not recorded in the financial statements themselves then they should be included as Notes more readily to identify and analyse net tangible assets per share and to report periodic profit and operational performance on realisations against cost, shorn of revaluations (Ryan, 1997);
- it was preferable to accelerate consideration of the measurement project and not pre-empt it (Ryan, 1997), nor to depart from historic cost in an *ad hoc* manner inconsistent with a conceptual framework (Paterson and Herbohn, 1997). One priority requirement should be to determine common capital and profit measurement criteria, including identifying operational performance and dividend-paying capacity (Priest, 1997; Ryan, 1997). It was misguided to report unrealised gains within income as being decision-useful (Clark *et al.*, 2002);
- the best measure of fair value is current value (Amen, 2000) which should be defined net of any selling and transport costs to market for any assets intended for immediate sale (Bourke, 2002; Woolf *et al.*, 2002). Agricultural assets should be no different to any other asset recorded under IAS 16, whether land, buildings or machinery, or for immature or mature assets or inventories recorded under IAS 2. For the latter, further costs should then be accrued to bring unfinished or immature products up to marketable condition (Amen, 2000);
- changes in carrying values should all be measured and reported in the same way for all agricultural and other assets and in the same location in the financial statements with changes recorded in reserves to provide a ‘firewall’ against dividend claims (Amen, 2000). Concerns were expressed that changes in carrying value components somehow reflect management performance if prices were derived outside of management control or as a result of management bias in surrogate measurements. These may lack credibility (Clark *et al.*, 2002), and be open to manipulation through time, creating unrealistic expectations about future profits and dividends (Priest, 1997; Ryan, 1997; Clark *et al.*, 2002; Woolf *et al.*, 2002). The only realistic performance measures were physical growth or numbers divorced from price effects (Amen, 2000);
- biological assets were no different to any other assets; all should be valued in the same way – at either fair value or cost and not with mixed-attributes, nor should specific valuation methods be required for some assets and not for others (Priest, 1997; Amen, 2000; Clark *et al.*, 2002). Ryan (1997) also criticised that the mixed-attribute model was being expanded from the balance sheet to the income statement;

- emphasis on agricultural management activity and decision-making was overstated. Ownership and control over assets was fundamental. The strange result of the standard was that native forest resources were excluded but plantations included (Paterson and Herbohn, 1997). In addition, standard setter's optimism was not shared by Paterson and Herbohn about availability of 'active and efficient' markets for SGARA assets, and if surrogates were used then reliability and inter-entity comparability suffered;
- valuation distinctions were apparent between livestock, bearer- and consumable-assets. Therefore different rules were recommended for each class, rather than the same for all, given each was clearly different, with different management objectives and time horizons. Some, *e.g.* bearer-fruit trees and vines, cannot be severed from land and sold. Their value lies in the productivity of future income streams through time. This is in contrast to (say) a tree which increases in value not only through growth and age, but also due to unwinding DCF-value effects over the diminished period to maturity and harvest (Clark *et al.*, 2002);
- as required for other assets, there was merit in identifying as current assets any biological assets, *e.g.* livestock, or growing inventory, *e.g.* lumber, expected by management to be sold within the next 12 months (Bourke, 2002; Clark *et al.*, 2002);
- concerns were expressed about requiring market valuation assessments at every balance date, including interim reports, assuming this were practical, absent evidence of impairment. This was not required for other assets such as intangibles, inventories, receivables and non-SGARA-fixed assets (Bourke, 2002; Clark *et al.*, 2002);
- in short, doubts were expressed whether a new standard for *Agriculture* was needed at all if existing standards were on a common basis once the measurement project was completed.

Earlier discussions have already identified issues for forestry in Australia preceding the issue of AASB 1037 (Herbohn *et al.*, 1998; Herbohn and Herbohn, 1999). These were later extended to issues requiring consideration and expected to apply when implementing AASB 141 in Australia (Herbohn, 2006), or IAS 41 further afield (Herbohn and Herbohn, 2006). Equivalent academic commentaries had occurred for crops (Cummings, 2000) and for other primary sector reporting entities in Australia (Dowling and Godfrey, 2001).

A robust critique emphasised the inappropriateness of the SGARA accounting model for the Wine Industry (Booth and Walker, 2003). This supported earlier academic articles. The critique was reinforced by practical experience in industry submissions to the AASB's AASB 1037 post implementation review. Each will be addressed in [Section 6](#).

### 5.5 Sir David Tweedie Identifies IAS 41 Agriculture for Possible Review

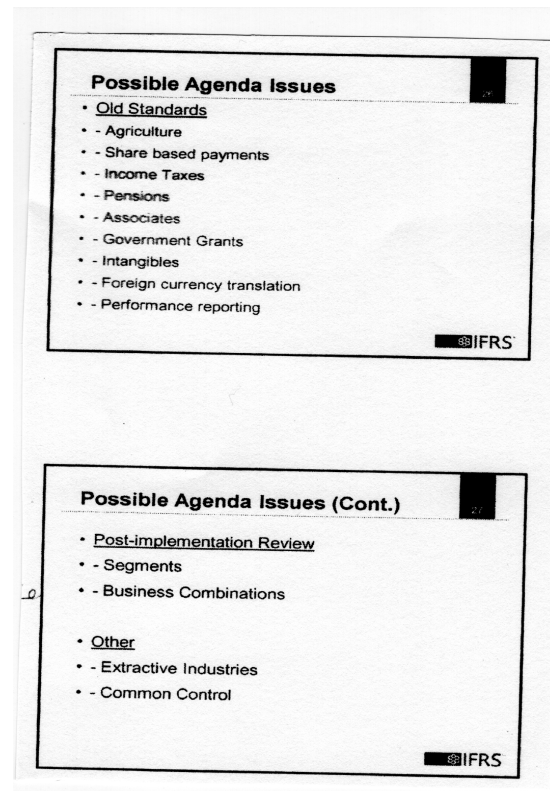
Sir David Tweedie made a special presentation to the New Zealand Institute of Chartered Accountants in Wellington during his visit in September 2010. The title of Sir David's address was *IFRS in 2011 and beyond*. His presentation contained some important messages. IFRS aimed to provide high-quality, transparent, and comparable financial information for investors and other users. These were best achieved by global standards adopted worldwide and founded on 'principles-based' rather than 'rules-based' standards. This would require reconciliation between the IASB and FASB under mutual Memoranda of Understanding.

Despite the above strategic objective, Sir David remarked there were "*some standards that are no longer relevant, conceptually incorrect or in need of overhaul*". In particular, at that time, the anomalous IFRS requirement for New Zealand, Hong Kong and South African reporting entities to record fictitious deferred tax liabilities that will never crystallise under current income tax legislation. Sir David recognised this was a problem under current IAS 12.

His presentation slides, Nos. 26-27, also revealed *Agriculture* headed the list of Possible Agenda Issues to be addressed in 2011-12 – "*agenda space permitting*".

Relevant to this topic, the list also included *Performance Reporting*, *Income Taxes* and *Post-implementation Reviews* – each continuing to be problematic to agricultural reporting entities and still unresolved IASB work-in-progress after nearly a decade.

**Figure 6. Possible IFRS Agenda Issues**



**Source: 'IFRS in 2011 and beyond'**

## Section 6. POST-ENACTMENT REVIEW

### Introduction

A post-enactment review (PER) assesses whether a project has met its objectives and planned deliverables. It can determine improvements to meet those objectives; and make recommendations for benefit of future projects thereby facilitating a ‘learning’ process. New accounting standards lend themselves to a PER but none has been reported. Table 31 summarises the PER rule-making process. A *post implementation review* (PIR) was the term AASB used for its formal review of AASB 1037. It is retained for this discussion.

***Table 31. Post-Enactment Review Rule-Making Process for Agriculture***

<b>Rule-Making Stage</b>	<b>Elements</b>	<b>Modes of Lobbying</b>	<b>Evidence</b>
<b>Post-enactment Review</b>	AASB issues PIR survey to assess impact of AASB 1037	Submissions on PIR	AASB Letter to IASB and survey attachment on reporting practices

Source: Table 1 modified for the AASB 1037 *Post Implementation Review* process.

In May 2003, following widespread concerns expressed about the *SGARA* standard in Australia, the AASB undertook a formal PIR on AASB 1037 *Self-Generating and Regenerating Assets*, also for the IASB’s benefit. The submissions and report have remained confidential, but a copy of both was obtained by application to the AASB.<sup>83</sup>

The review was completed and forwarded to the IASB on 25 November 2003. The AASB’s PIR cover letter to the IASB contained the unexpected recommendation:

**The AASB project staff believes there is merit in excluding bearer-SGARAs and entities with vertically integrated operations from the scope of IAS 41 for the reasons stated (AASB, 2003, Nov., p. 3).<sup>84</sup>**

However, to date, the IASB has retained the IAS 41 standard intact, apart from the International Financial Reporting Interpretations Committee’s (IFRIC) recommendations to the IASB, and supply of operational interpretations and guidance. These are discussed below.

<sup>83</sup> All information in this Section is derived from papers requested from the AASB in August 2007.

<sup>84</sup> Refer [Appendix 21](#), page 98.

## **6.1 Background to the AASB's Post Implementation Review (PIR)**

At its Board Meeting in May 2003, whilst Keith Alfredson was Chairman, the AASB considered it opportune, given up to two years experience with the AASB 1037 *SGARA* standard, to review the new standard and to determine likely implementation issues for Australian entities on transition to AASB 141; also to provide feed-back to the IASB, at the IASB's request.

The PIR concept was not new. In its original *Project Brief* the AARF required Roberts/UNE to '*undertake a detailed review on the topic of self-generating and regenerating assets...overseas as well as Australian literature...and the professional pronouncements (and post implementation reviews) of all major overseas bodies*' – refer Appendix 6, p. 16, para. 1. None was reported in the DP 23 Report.

The AASB's PIR was issued with the ED 114 to transition from AASB 1037 to the harmonised AASB 141 version of IAS 41 *Agriculture*. Taken together, the aim was to determine potential improvements to IAS 41 and to advise the IASB accordingly. At the time the IASB was not intending to review experience with IAS 41 until after 2005.

ED 114 was issued on 7 May and the PIR on 16 May 2003. The response due date was 30 June for each. There were comparatively few responses, possibly because of the relatively short report-back period prior to the financial year end. Whilst Appendix 17 contains the list of ED 114 respondents, those for the PIR remain confidential apart from generic classifications for 'preparers', 'valuers and auditors', and 'other users'.

A precursor to initiating the PIR process may have been the continual adverse comments about AASB 1037 during 2002/03 by preparers in Interim and Annual reports, academic articles and journalists in the financial press. Foster's Ltd. and Southcorp Ltd. individually, and through The Group of 100, had made critical representations direct to the AASB.

For example, following publication of Foster's Ltd. June 2002 Annual Report, the CFO, Trevor O'Hoy, wrote to the AASB Chairman, Keith Alfredson, on 23 August 2002 recommending the *SGARA* standard '*should be adjusted to exclude the impact of this*

*standard on the wine industry*'.<sup>85</sup> O'Hoy raised the matter again, forcefully, with Ms Ruth Picker then the AASB's Acting Chairman, who was invited also to attend the writer's Delahunty Trust Project meeting at Foster's Ltd. on 15 October 2002 (Milne, 2004).

Foster's Ltd. then followed up with another letter to the AASB on 10 December. The general tenor of Foster's Ltd. representations can be gauged from its conclusion:

the accounting requirements and valuation concepts when applied to the wine business are too complex for the average user, including analysts, of financial statements to understand especially as the major performance indicator is based upon the entity's cashflows which SGARAs do not impact upon until sold. Given that analysts reverse out, and ignore, the effects of SGARA accounting, Foster's now presents its financial results to the investment analysts excluding the effects of SGARA leading to their question "what purpose this standard serves?"

The PIR questionnaire was devised to obtain a better understanding of such issues.

In summary, respondents expressed concerns about the usability and practicality from actual experience with AASB 1037 and the consequent lack of reliable, comparable and consistent financial statements for reporting purposes between reporting entities.

The PIR cover letter was sent on 25 November 2003 to Sir David Tweedie, Chairman of the IASB by Ms. Monique Ledden, Project Manager, on behalf of the AASB. It is reported in full as Appendix 21. It contains AASB recommendations and its PIR survey report.

The AASB, and IASB, were probably surprised at the resulting conceptual criticisms and practical failures in the operations of AASB 1037 as a 'high quality' standard reported in detail in Appendix 22B. It is not surprising that the PIR has remained confidential.

The IASB has taken no direct action on the AASB's research initiative, nor recommendations, ostensibly because of higher priority items taking precedence in the IASB's agenda setting and its annual improvements work programmes.<sup>86</sup>

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<sup>85</sup> Refer Appendix 19, p. 95. This letter was also copied to the MD/CEO of 16 other Wine Companies.

<sup>86</sup> IASB representatives, Messrs Warren McGregor and Tatsumi Yamada, confirmed this at a National Assn. of Accountants breakfast seminar held in Sydney on 6 November 2008.

## **6.2 PIR Questionnaire and Request for Submissions**

The AASB initiated the PIR at its May 2003 meeting. Its PIL Strategy Agenda Paper was updated progressively *e.g.* as Agenda Paper 6.5.2 for the September meeting – refer Appendix 22A.

The Introduction summarised the need for reporting entities already complying with AASB 1037 to migrate to IAS 41 for financial years commencing on or after 1 January 2005. At that stage there were no known early-adopters of IAS 41 in Australia so no implementation issues had been identified.

However, Foster's Ltd. had twice written to the AASB expressing critical views about AASB 1037, specifically that the existing standard should be amended to exclude the wine industry, as a bearer-SGARA industry.

AASB staff, and Board members, therefore considered it timely to review and seek feedback on actual implementation experience to date. The IASB had also sought advice on the outcome of the proposed review. The AASB therefore extended its mandate to include identification of potential problems with and improvements available for IAS 41.

Staff prepared a draft questionnaire. This was pilot tested by Southcorp Ltd. to ensure it addressed all expected relevant issues.

The AASB Board sought to canvass a wide range of experience. The recommendation was to approach a number of interested entities and individuals amongst Preparers of Financial Statements; Auditors; Valuers; Users; Academics and Representative Bodies. For comprehensiveness, the questionnaire was designed to disaggregate Preparers to differentiate between Private *vs.* Public entities; Bearer *vs.* Consumable industries; short *vs.* long term operations; and, vertically integrated *vs.* stand-alone operations.

### 6.2.1 PIR Survey Questionnaire

The ‘Preparer’ Survey was segregated into three parts with an extensive range of questions/sub-questions for each Part, a total of up to 95 questions – but longer for entities with more than one SGARA-type.

The Parts comprised:

- A. General questions about the entity – 4 questions, and 14 sub questions;
- B. Questions on each type of SGARA for each of the standards -  
with 14 questions and 48 sub-questions – and with a separate series of responses requested for each SGARA type; and
- C. General questions on how the respondent thought SGARAs should be accounted -  
with 9 questions and 16 sub-questions.

There were separate surveys for ‘Auditors and Valuers’ as one category and for ‘Users’ as another. The response summaries in [Appendix 22B](#) indicate the following sections:

- A. Information about the respondent (requested from all respondents);
- B. General Comments on the Standards (from Users);
- B. Valuation methods for different types of SGARAs (from Auditors and Valuers);
- C. Scope of the Standards with any special entity or industry features  
(from Auditors and Valuers);
- D. Presentation and Disclosure requirements (from Auditors and Valuers)

As an overview, the AASB’s internal final Survey Report summarised the aggregates of Questionnaire Invitations sent out and Responses received:

**Table 32. AASB - PIR Survey Report Summary**

Category	Description	Questionnaires sent out	Responses received	%
P	Preparers	82	15	18
AV	Auditors and Valuers	12	6	50
U	Users	15	5	33
<b>Total</b>		<b>109</b>	<b>26</b>	

Source: AASB Survey Report [Appendix 22B](#), p. 110.

The disappointing response rate by SGARA Preparers should not go unremarked.



This continued a pattern already observed in responses in Australia to DP 23 and ED 83 requests and for the IASC's DSOP and E65. It may reflect a 'free-rider' lobbying effect (Sutton, 1984). Small/Medium-sized wine companies may have decided not to participate since they expected and/or knew, for example, either Foster's Ltd. or Southcorp Ltd. would make a full submission, or an industry 'Vintner/Distiller' body would submit a group response. Another reason was that the short response period for a lengthy survey which coincided with post-harvest and pre-financial year-end closure routines.

An alternative view is that potential responders were satisfied with the standard (Beresford, 1993). However this is unlikely for bearer-SGARA preparers given the concerns and issues raised by those who did respond and as expressed in Annual Reports. There were two other possibilities. Some preparers had already reached accommodation with their auditor to ameliorate the standard's 'worst' effects, and were not willing to expose this. Alternatively, potential responders regarded the PIR as lacking in transparency given the confidentiality requirements imposed without any AASB commitment that survey results would be published, or acted upon. As proved to be the case.

### **6.2.2 Analysis of Submissions**

The commentary below is derived from the AASB staff's high-level summaries of PIR responses in Appendix 22B. Staff described current practice noting some positive aspects and many reported problems experienced with AASB 1037, or expected from IAS 41. The issues are presented here for respective responder groups, but with separate comment recorded about special concerns expressed in submissions. References below relate to page numbers in Appendix 22B.

There were submissions from 15 'Preparers', of which two were from the public sector and one was a wine industry representative body; from five 'Auditors' and one 'Valuer'; and from five 'Users'. Responses covered the following SGARAs:

- Consumable SGARAs: Crops (cotton, onions, carrots, salmon, fruit/nuts, olives, apples, walnuts, cherries); Livestock (swine, trading cattle and sheep) and Forests/Forest products;
- Bearer SGARAs: Grape vines, Orchards, Breeding cattle and sheep.

### **6.2.2.1. Preparers** (Appendix 22B, pp. 111-46)

#### **A. High Level Staff Summaries**

- a) Measurement and Recognition (pp. 116-7):
- Problems with valuations: these included the costs incurred with external consultants, management and auditors/valuers and time spent resolving the subjective differences of opinion between each; and the estimation of yields/assumptions to be used in valuation models; with little or no information-value added to the resulting financial report;
  - Interpretation of IAS 41:21 of whether future growth should be included in valuations: there may be material forestry write-downs if future growth remain excluded from NPV calculations, with significant compliance costs involved;
  - Reliability of valuations: whilst 10 believed SGARAs can be valued reliably, there were two who did not believe valuations were reliable and another with misgivings on reliability for determining for grape vines and cotton values under the standard
- b) Scope of Standards (pp. 137-9):
- seven responders believed there should be no exclusions from AASB 1037 scope whereas seven believed harvested grapes, bearer-SGARAs and livestock traded on open markets should be excluded because cost outweighed benefits; of these, two stated no exclusions should occur for IAS 41;
- c) Special industry/entity features (p. 140): the seven entities who indicated costs of SGARA accounting exceeded benefits identified particular reasons for:
- wine companies due to their vertically integrated operations;
  - annual crops/products with short life cycles and companies facing volatile pricing; and
  - small companies;
- d) Presentation and disclosure (pp. 141-6). There were mixed responses on whether current disclosures were useful to users of financial reports. Specific issues were the difficulty in obtaining information; the ambiguity in disclosure requirements; potential disclosure of commercially sensitive information; and misleading information through not differentiating realised and unrealised income.

#### **B. Salient Issues Recorded from Consumable-SGARA Preparers' Submissions**

Agricultural Products: SGARA accounting caused confusion for shareholders and financiers alike since it was contrary to traditional accounting methods for establishing reliable profit measurement and to determine operational performance;

Cotton: mixed valuation methods ranged from cost, NMV in active markets and cotton futures as some crops were sold years ahead; valuations were not regarded as reliable for unsold cotton, because of anticipated yields, production and future realisations;

Forestry: respondents adopted a variety of valuation measurement assumptions.

DCF modelling used either pre-tax or after-tax assumptions; discount rates were based on either industry benchmarks or internal WACC with risk adjustments in discount rates or in future cash flows for growth/yields and with projection periods ranging from 10 to 90 years. Prices used in models were at averaged past period prices, current levels or estimates for future periods, and for future growth;

Livestock: the standard was regarded as workable if financial statements can be interpreted alongside market information, but the exercise was complex and less useful for users - who ask “*why do you book profits before the livestock is sold?*”;

Salmon Farming: currently used cost for <2kg fish and NMV for > 2kg for salmon or other fish; but, because of difficulty in determining market prices reliably, P-5 proposed reverting to cost;

Valuation issues for Livestock traded on open markets:

- the effect of the standard was to recognise profit (or loss) before it was actually realised, and it may never be realised;
- the cost of information disclosure outweighed the benefit because:
  - valuation was unreliable in volatile markets due to unpredictable price changes;
  - treatment was inconsistent with other trading stock items, like stock feed; and
  - period-end livestock values would differ from realisations when stock was eventually sold, and when users analyse results against later prevailing prices.

### **C. Salient Issues Recorded from Bearer-SGARA Preparers’ Submissions**

1. Wine Companies and Wine Industry Group: Each advocated removal from reporting application under the Agriculture standard. Issues included:

- interim revenue reporting of unrealised values for grapes and vines prior to harvest was very uncertain as to yield, quality and market prices, thereby potentially misleading to investors;
- obligation to create and report unrealised inventory accounting profits for integrated wine entities for up to 3 years (wine) and 4-40 years (fortified wines) before final sale realisation;
- a vine was a depreciating asset, as was recorded prior to AASB 1037, and so can be adequately accounted under equivalent IAS standards to AASB 1010 and 1021;<sup>87</sup>
- fair valuing vines was imprecise and subjective because they were not traded as stand-alone assets separate from the integrated vineyard, there were no markets for them;
- strong opinions were noted that vines should be valued on a modified-historic cost basis to align with other integrated vineyard assets;
- bearer-SGARA valuations were a highly subjective derived figure, inhibiting reliability of measurement and comparability between entities;

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<sup>87</sup> AASB 1010: *Accounting for the Revaluation of Non-Current Assets* and AASB 1021: *Depreciation of Non-Current Assets*.

- concern that IAS 41 disclosures can result in identification of commercially sensitive vineyard costs and profitability, unlike for other industries;
- users and analysts generally excluded the impact of SGARA accounting when analysing financial results; accordingly, Preparers presented financial results which exclude or report all the adjustments required to be made for non-realised SGARA entries; and
- the consensus was that AASB 1037 did not provide users with useful information which justified the cost, time and effort of obtaining it; this was expected for IAS 41 too.

## 2. Orchard & Fruit Tree Companies used various valuation and measurement criteria:

- an NMV for similar or related apple tree assets determined by an independent valuer with valuation recorded by deduction of land/buildings from the total orchard value; and
- pre-tax, industry-benchmark or risk-adjusted discount rates, with risk-adjusted yield cashflow assumptions to determine NPVs over 3-33 year projections (depending on type of orchard), with conservative price forecasts.

### **6.2.2.2. Auditors & Valuers** (pp. 147-161)

There was a submission from one Valuer and five Auditors – two as a firm, three as individuals. Auditors undertook audit and valuation reviews for Consumable-SGARAs (livestock, forests and fruit/nut crops) and for Bearer-SGARA entities (vines and orchards).

#### **A. High Level Staff Summaries**

- a) General Measurement and Recognition (pp. 150-1): There was an extensive summary of general problems elaborated below in auditing in applying auditing requirements and in making NMV valuations or auditing them under AASB 1037;
- b) Disclosure Requirements (p. 161): Two believed AASB 1037 requirements were too complex and extensive; but reduced to one for less onerous IAS 41 disclosures.

#### **B. Salient Issues Recorded from Auditor and Valuer Submissions**

There were concern about the quality of revenues, earnings and asset values due to:

- the nature of evidence required to support the validity of assumptions, *e.g.* discount rates, where a small change in a rate yields large value impacts;
- determining appropriate separate values for land, improvements and long-term SGARAs;
- definition of SGARA revenue as clients include both the change in asset value as well as product sale proceeds from that asset, potentially duplicating revenue;
- further guidance needed where a firm contracted prices exist that exceed actual product market prices at a balance date;
- hard to track and understand different effects on revenue and profit through time; and
- preparers' focus on cashflows and reporting pre-SGARA EPS and KPI metrics.

### Measurement and Recognition Issues

For Interim Reporting: there was unwarranted audit review and reporting risk where values were subjective estimates for yield, quality and quantity parameters and subject to smoothing bases for seasonal variation. Preparers tended to be conservative in application of NMV pre-harvest. The capitalised immature inventory cost was incorporated into the SGARA asset value. This reduced risks of discrepancies for subsequent climatic and pest events for harvested product yields and on SGARA end-asset values determined at year end;

For Crop and Livestock Consumable-SGARAs: significant arbitrary audit management judgment was required to be exercised, from insufficient audit evidence to determine current market values of various livestock and crop asset classes; for cost of transport to market in multiple market locations, and from variable changes in market prices for different economic and climatic conditions during harvest across locations - some within Australia, some overseas;

For long term Bearer- (vineyard) and Forest-SGARAs: SGARA valuation was an arbitrary estimation process to separate its value from a combined valuation of bare land, improvements, or any trellising and irrigation systems. For Forest-SGARAs a wider industry and forestry knowledge was required for audit valuation verification for timber plantations generally, for native forests managed on a sustainable yield basis in order to determine timber deemed available for sale at time of valuation, and for identifying and separating out restricted forests;

General Valuation issues: responses identified considerable variations in assumptions for NMV determination between identifying NMVs in active and liquid markets, between assumptions in values for immature crops measured at cost, for types of discount rates used in models, and for differing time periods used in those models.

#### **6.2.2.3. Users** (pp. 162-70)

There were five respondents: a conservation group (U-2) - primarily interested in native forests; two academics U-3 and U-7; the Tasmanian Auditor General (U-6 - responsible for assessing stewardship of the Tasmanian Forests by the Tasmanian Forestry Corporation); and U-9, an Analysts representative body.

#### **A. High Level Staff Summaries**

a) Scope of standards: there were two responses. One believed all forests should be included in AASB 1037, but the other believed it should not apply to old-growth forest held for clearing. Because of more robust definitions in IAS 41 the latter's position reversed because deforestation was excluded as it represented extraction from, not management of forests or re-growth (p. 165-6);

b) Special industry features: one respondent (the Tasmanian Auditor-General) noted state forestry corporations have been unable to apply AASB 1037 without material errors in calculation of SGARA values which affects usefulness of the

information. That respondent also questioned the usefulness of assessment of stewardship of SGARA assets (pp. 167-8);

- c) SGARA accounting vs. lease accounting: academic respondent U-7 considered AASB 1037 accounting more useful because capitalisation of executory contracts is based on a misconception relating to profit measurement (p. 164);
- c) Presentation of revenues and expenses: U-7 also believed the assumed purpose of money capital maintenance and profit measurement should be based on executed sales contracts and so capture realised profits (p. 169);
- d) Disclosure requirements: respondents raised the following issues (p. 170):
  - failure to separate asset types, disclose sensitivities and assumptions under AASB 1037;
  - requirement to disclose biologically mature from immature assets under IAS 41; and
  - cost-based amounts (for profit measurement) and current market selling prices (for wealth measurement) should be separately disclosed under AAS 1037 and IAS 41.

### **B. Salient Issues Recorded from Users' Submissions**

- a) Academics: U-7 considered IAS 41 is too limited in its SGARA definitions and should conform to the more comprehensive AASB 1037 definitions;
- b) Representative Body for Users (U-9): analysts expressed concern about classification of realised and unrealised value increments as income without separate component disclosures. If there were a choice, they sought only to report realised revenues as income. UK Investment entities were required to adopt mark-to-market reporting with value increments in three matrix columns (Realised, Unrealised, Total). This might be applicable for IAS 41 Agriculture.<sup>88</sup>

#### **6.2.2.4. Summary**

Although Appendix 22B provides high level staff summaries and other salient staff comments it only represents a distillation of more comprehensive responders' submissions, withheld under confidentiality. This internal PIR Report was itself confidential. However, similar to the IASC's Field Test Report, it indicates the extent of internal dialogue between

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<sup>88</sup> A variant of this matrix-type reporting was adopted by four U.K./European-based Palm Oil/Rubber Plantation companies and a N.Z. Wine Company. Refer to the discussion in [Section 5.3.4](#).

staff and Board, hitherto unreported publicly, and the difference in scope to the *SGARA/Agriculture* standards approved by respective organisations.

The AASB, and later the IASB, should have been concerned about the number of theoretical and practical issues raised and problems experienced from a cross-section of Preparers, Auditors and Users. A feature was the inconsistent methods and bases revealed to determine surrogate net market values. In particular, strong representations were made by vertically integrated wine companies that the standard should not apply to them for many of the reasons described previously and also elsewhere in academic submissions.

Indicative of the *inside access* model is the secrecy accorded the PIR. Ruth Picker's 2003 Acting-Chairman's AASB Annual Report referred to ED 114 convergence (FRC, 2003, Appendix F), but contained no reference to the contemporaneous PIR Survey. David Boymal's 2004 Chairman's Report and Appendices made no reference to the survey results. However, Boymal did note without elaboration in his 2004 FRC Report:

in the course of preparing Australian versions of the International Accounting Standards the AASB identified a number of problems and inconsistencies in the original International Accounting Standards. The IASB was progressively informed of these findings, many of which were rectified by IASB before its 'stable platform' of 2005 standards was finalised (p. 19).

One that was not 'rectified' was IAS 41. Publicly, the PIR went unreported...except for the reference by AASB staff which was minuted during the October 2004 FRSB meeting considering NZ IAS 41, referred to above.

### **6.3 PIR Sequels**

#### **6.3.1 AASB Letter to the IASB – IAS 41 Agriculture Recommendations**

The letter addressed to Sir David Tweedie, as IASB Chairman, combined the results from the AASB's ED 114 submissions on AASB 1037 convergence onto the IASB's IAS 41 *Agriculture* standard, and the summarised results of the PIR, the full PIR report and associated AASB recommendations (AASB, 2003, Nov.). The AASB's stated objective for presenting the PIR was to help improve effectiveness of the IASB's IAS 41 standard.

The AASB letter has remained confidential. In turn, the IASC has never referred to it. This might be attributed to the principal controversial recommendation that the standard should no longer apply to integrated bearer-SGARA wine companies. This was foreshadowed in Keith Alfredson's ED 114 response noted earlier.

The letter, in [Appendix 21](#), covers each set of findings:

#### **6.3.1.A. Comments on and outcome of the ED 114 Request for Comment**

The Board advised it had decided to continue adopting IAS 41 without amendment, although, as noted previously, the grammatical style was altered.

However, the AASB proposed to transfer from AASB 1037 the physical quantity reconciliation disclosures into the Australian equivalent for IAS 41:43 denoting the 'animals' or 'plants' disclosures within bearer- and consumable-SGARAs.

The AASB also proposed to transfer from AASB 1037:7.1(b) disclosures on the nature and extent of SGARA asset restrictions on use or outputs.

The AASB expressed the hope the IASB would consider adopting those disclosures when IAS 41 was next amended. The IASB did not do so. As a result these changes were removed from AASB 141 on recompilation in 2006.

#### **6.3.1.B. PIR and IAS 41 Convergence Issues**

The purpose of the PIR was *'to establish which Standard is superior and whether either or both Standards require review in the short term and in the longer term'*.<sup>89</sup> For example, one specific issue raised by respondents was IAS 41:21. The effects of future growth were required to be excluded in a DCF valuation calculation. The AASB noted the matter had been referred to IFRIC for consideration.

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<sup>89</sup> Refer to the last paragraph: Scope of Project on page 102 in [Appendix 22A](#).



The AASB identified some entities where application of SGARA accounting under IAS 41 was now considered inappropriate. For others, costs were assessed to outweigh benefits. The recommendations covered:

1. Wine Companies with vertically integrated operations. Profits and losses were prematurely recognised given the wine is sold many years later. Therefore, endorsing wine company submissions, the information is of no benefit because it runs counter to the business purpose of establishing integrated operations from vineyard through to final wine markets;
2. Consumable SGARAs for annual crops. Strict SGARA accounting is inappropriate for short life-cycle crops. Actual realised proceeds should be substituted for less reliable fair value measurement recognition;
3. Bearer SGARAs, e.g. grape vines. These were considered akin to IAS 16 *Property Plant and Equipment* and should be carried at cost, or modified-cost, less accumulated depreciation and impairments.

Because SGARA fair values cannot always be measured reliably in the valuation process, the rebuttal presumption in IAS 41:30 should apply to them so that these bearer-SGARAs could be removed from IAS 41 as beyond its scope;

4. Small Companies. Respondents believed the cost of SGARA accounting did not provide great benefit to users; the AASB recommended this issue be addressed by the IASB's *Small and Medium-sized Entities* (SME) project.<sup>90</sup>

Based on the outcome of the PIR Survey, the AASB recommended a number of other changes in the scope of IAS 41, including accounting for Leases involving SGARAs and for certain additional disclosure amendments. The AASB concluded by urging the IASB to consider their comments as soon as possible and offered to assist in that review.

### **6.3.2 Outcome of the PIR Letter Recommendations by the IASB.**

The original intention was that the IASB would undertake a review of IAS 41 after 2005. That review has not yet occurred due to higher agenda priorities.<sup>91</sup>

<sup>90</sup> Possibly because of Paul Pacter's leadership consultancy role in developing the SME Project, there was only minimal change to IAS 41 requirements within the SME standard when issued in June 2009.

<sup>91</sup> Refer Section 5.5 (p. 233) - Sir David Tweedie did suggest in Wellington, in September 2010, the standard could be reviewed in 2011-12, agenda space permitting.

### 6.3.3 Consideration of Other Matters in the AASB Letter

#### 6.3.3.1. IAS 41 Interpretations Added to IFRIC Agenda.<sup>92</sup>

IFRIC considered a number of issues arising from IAS 41 over the period September 2003 to January 2007. These emphasise that IFRIC was effectively also a *de jure* quasi-standard setter in terms of rule-making political processes. It stood alongside the IASB. Its interpretations and guidance had full effect for auditors and preparers. It could also refer recommendations for formal IASB consideration, *e.g.* in an Annual Improvements project.

However IFRIC determinations proceeded at a measured pace; not always reaching resolution.

The eight IAS 41 topics on which IFRIC has deliberated or been requested to provide guidance were:

**A. IAS 41:21** - removal of future biological growth from fair value determination.

IAS 41:21 was added as a result of the IAS 41 approval compromise. It read:

the objective of the calculation of the present value of expected net cash flows is to determine the fair value of a biological asset in its present location and condition...the present condition of a biological asset excludes any increases in value from additional biological transformation and future activities of the enterprise, such as those related to enhancing the future biological transformation, harvesting and selling.

In September 2003, IFRIC agreed the clause was internally inconsistent and that risk-adjusted growth should be included within any DCF valuation calculation. In December 2003, it was referred to the IASB to clarify the clause in its next IAS 41 Improvements Project. On further consideration, in February 2004, IFRIC agreed fair value should include all discounted risk-adjusted expected future cash flows associated with successful biological transformation prior to harvest, and proposed to draft an amendment to IAS 41.

With lack of progress, the AASB Chairman sent a letter to IFRIC in August 2005 noting the difficulty in getting responses if IFRIC met only seven times a year; that *'IFRIC could not endorse particular domestic interpretations by particular*

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<sup>92</sup> These comments are sourced from the Deloitte IAS-Plus International Accounting Standards website: IFRIC Agenda for IAS 41: Fair Value Measurement Issues in Agriculture

*countries...Australia may have to make its own interpretations'* as reported by Gettler (Gettler, 2005, August) and ACFA (2007, July, p. 5).

At its November 2006 meeting, IFRIC endorsed removal of the prohibition against taking into account future growth. In January 2007, IFRIC approved an amended text and recommended the IASB Board remove the prohibition on taking into account future biological growth.

First referred in 2003, the outcome of IFRIC's deliberations was eventually submitted to the IASB in 2007 for final approval. The agreed effective date was 1 January 2009.

Indicative of IFRIC/IASB deliberation processes, the final text of the agreed Minute at the March 2008 IASB Board meeting approving the amendment was:

***Analysis of Comments on the Improvements Project Exposure Draft***

This session was a continuation of the re-deliberations from the February Board meeting on the Annual Improvements exposure draft published in October 2007.

***Biological transformation (IAS 41)***

The amendment proposes to remove the prohibition on taking 'additional biological transformation' into account when determining fair values using discounted cash flows.

Respondents that were not supportive of the amendment highlighted that it would conflict with the objective of measuring the fair value of the asset in its current location and condition. Other respondents expressed concerns over the proposed inclusion of harvesting in the definition of biological transformation on the basis that harvesting is carried out by humans and is therefore not part of the biological transformation process.

The staff proposed to finalise the amendment but to make the following changes to the ED:

- expand the Basis for Conclusions to make clear that the reason for using a discounted cash flow model is to estimate a market based value of the asset in its current location and condition;
- remove the word harvest from the proposed change of the definition of 'biological transformation' and replace the term 'biological transformation' with the term 'biological transformation or harvest' throughout the standard where appropriate;
- require prospective application of the amendment.

One Board member recommended that the clarification in the first point would be better placed in the main body of the standard. Staff agreed to change the drafting accordingly.

*Final Improvements Issued May 2008*

On 22 May 2008, the IASB published final amendments to 20 IFRSs, including IAS 41:21, and the related Bases for Conclusions and guidance, resulting from the Board's Annual Improvements Project for 2007...(this) Project provides a vehicle for making non-urgent but necessary minor amendments to IFRSs. The effective date for most amendments is annual periods beginning on or after 1 January 2009.<sup>93</sup>

**B. IAS 41:22**:- valuation treatment for current fair values for future re-planting obligations or requirements for future obligatory land restoration.

This item was initially considered at IFRIC's September 2003 meeting. It concluded any replanting provision should be raised at felling, not at planting. Land restoration was addressed at the December meeting noting equivalence to asset decommissioning. In February 2004, IFRIC considered that where the restoration will create an additional asset, it should be capitalised but if land restoration occurred on leased property, expenditure should be expensed. Finally, in November 2006, IFRIC decided not to issue guidance on accounting for obligations to replant a biological asset after harvest.

**C. Determination of Fair Valuation for Biological Assets and Produce**:

In February 2004, IFRIC determined that selling and transport costs should be deducted from active market prices to measure net fair value measurement at the 'farm gate'.<sup>94</sup>

**D. IAS 41 Biological Produce to be Valued at 'Highest and Best Use'**:

At its May 2004 meeting, IFRIC agreed that the 'highest and best use' principle, as used in property valuations, should be the assumed fair value price at harvest since that was the rational economic choice if biological produce were of sufficient quality.

**E. Relevant Fair Value Basis If No Market Exists for Immature Quality Produce**:

At its May 2004 meeting, members confirmed a nil value was inappropriate and *'that the value of unripe grapes should be determined by reference to the price of ripe*

<sup>93</sup> In reality, preparers and auditors had adopted this practice ever since the IAS 41 effective date in 2005.

<sup>94</sup> This agreed with the AASB 1037 practice and was an endorsement of the AASB's IASB E65 submission.

*grapes*'.<sup>95</sup> But no conclusions were reached on how to determine values at intermediate ages where markets only exist at specific ages - other than to request IASB assistance.

**F. IAS 41 Biological Asset Valuation 'At Highest and Best Use in the Most Advantageous Market':**

The November 2006 meeting noted this was appropriate for inclusion within the IASB Discussion Paper on *Fair Value Measurement* even though it may reappear as a future agenda item.

The last recorded IFRIC meeting dealing with IAS 41 matters was in January 2007 at the conclusion of which members agreed to remove *IAS 41 Agriculture* from their agenda. This was an example of a formal termination in agenda-building processes (Cobb and Elder, 1983).

**6.3.3.2. Small and Medium-sized Entities (SME) Project**

The project commenced in July 2003 (Singh and Newberry, 2008). IASB published the SME standard in July 2009 on completion of all agenda consideration stages. Two identified simplification issues relating to IAS 41 were proposed for the SME project.

**A. IAS 41 Requirement for Agricultural Produce Not Applicable to SMEs**

The proposal was to use a cost model for all agricultural produce. This was rejected because not only was 'fair value' generally regarded as more relevant, but quoted prices were deemed generally available in active markets – and measuring cost was regarded as burdensome and arbitrary because of allocations required.

Few SMEs would accept these propositions. The standard setters have treated all SGARAs as equal, thereby failing to distinguish between different sectors and between bearer- and consumable-SGARAs.

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<sup>95</sup> This was an Interim Reporting issue. The observation provided no assistance. It was the reason for the initial query. In practice, as reported in company Accounting Policies, guesstimated surrogate or 'capitalised cost' was used - because any other valuation basis was regarded as impractical and unreliable.

### **B. Determination of Fair Value for Agricultural Assets**

The SME standard required an entity to determine whether fair value was capable of determination without undue cost and effort. If it can be determined, full IAS 41 will apply with full disclosures; if not, fair value should be deemed at cost less accumulated depreciation with relevant disclosures.

Australia and New Zealand have not yet accepted the SME standard; instead each prefers, for the meantime, to maintain their differential reporting concessions; *i.e.* use of cost even where fair value can be reliably measured; and the continued use of taxation standard values for classes of livestock as a proxy for fair value.

### **6.4 Contemporary Confirmation of Respondents' Concerns**

Two independent commentaries had reached similar conclusions prior to the PIR survey. The first was a journal article *Valuation of SGARAs in the Wine Industry: Time for Sober Reflection* (Booth and Walker, 2003); the second was after the writer undertook field-work in 2002/03 into how the new SGARA standard was progressing in Australia.

#### **6.4.1 Booth and Walker Article**

This article supplied a critique of AASB 1037 specifically for bearer-SGARA assets, *i.e.* vines in vineyards, which became non-viable if severed from agricultural land. This was in contrast to consumable-SGARAs, like livestock. Booth and Walker referred to the 'startling' logic in DP 23 that all bearer assets were equivalent to plants and trees. On the contrary, they retain their value only when integrated with their *terroir* (2003, p. 53).

However, both types of SGARAs were valued under AASB 1037 on the same net market value basis. If the bearer-asset were severed from the land, it then ceased to have any viability value and no market for it in that form as a SGARA, other than as waste wood. Furthermore, whilst a consumable-SGARA ceased to exist when harvested, the vine bearer asset continued to exist after a harvest, for future harvests, with its annual grape produce then being a consumable-SGARA in its own right (*ibid.*, p. 54).

The standard went further. The change in NMV carrying value was treated as an element of net profit, and distributable as such, either as the value of annual produce at point-of-harvest, realised or not, or as a non-cash net asset revaluation/impairment – in contrast to the supporting integrated land and infrastructure whose value increments/decrements were accounted as movements to/from reserves (*ibid.*, p. 55).

The value of the bearer-SGARA, the vine, was regarded as suspect when determined under the required methodology in respective AASB 1037 and IAS 41 standards.

Booth and Walker analysed the defined measurement valuation bases. NMV by definition was an ‘exit value’ representing the net amount expected to be received from disposal in an active and liquid market. But the asset had no exit-value, since there is no market for it; nor is there an entrance-value (*ibid.*, p. 55). A vine or apple tree when severed from its *terroir* cannot be sold, or bought, as a viable asset. It therefore had no reliably measurable value other than a nil value. Ascribing any other direct value to the bearer-SGARA was ‘*simply a false statement*’ (p. 59).

The standard, as eventually developed, identified alternative measurement bases. Traditional practice was that net development costs were accumulated as a permitted asset valuation basis, including capitalised interest, subject to an impairment test against recoverable market value for the combined vineyard value (*ibid.*, p. 54). But it need not be. A wine company can undertake a DCF ‘surrogate’-NMV vines valuation calculation at initial planting when cost was minimal. The seedling then would carry the full discounted NPV value of its assumed lifetime-yield at forecasted net proceeds and viticultural costs from inception. There would be no proven produce yield until commercial maturity at least three to four years later, and – apart from time-discounting effects - the then full NPV value could be reported as net revenue within profit from the date of planting (p. 57).

More usually, in practice, valuations would change from cost to fair value assessment at vine maturity once commercial production started. That will depend on whether:

- the asset valuation is determined by a net cashflow discounting method which in turn is a function of many subjective management, or directors’, assumptions about future yields, prices, costs, discount rates and useful life. This disclosure in all its complexity is seldom supplied making independent analysis or verification difficult; or

- the combined integrated asset is valued independently at prevailing market value and from that value the current assessed values of land and infrastructure assets respectively are deducted leaving the bearer-SGARA asset value determined-by-deduction as the '*fiction [of] an exit value for mature vines*' (*ibid.*, pp. 53-8).

This methodology represented a mixed-measurement valuation system since not all component values were identically determined: some may be valued at market value and some at input replacement cost, with no allowance for 'intangible' *terroir*, such as appellation market goodwill for the bearer-asset or for viticultural management skills.

Booth and Walker concluded that '*to assign the residual value and call that net market value is simply [another] false statement*' (2003, p. 59). They noted with approval similar comments from ED 83 respondents.

They also identified the special measurement issues for interim reporting. The implications were not considered in the standard, even though the standard envisaged full valuations were required for each reporting period, including interim reports.

This issue was especially acute for bearer-SGARAs. At the half-year, the grape crop is immature. There is no valid market, by definition, even if veraison has occurred. The future crop is still attached to the vine, not available for sale as inventory, as might be the case for interim reporting for some consumable-SGARAs *e.g.* for livestock. Differing practices were identified, including cost or rule-of-thumb estimates for forecasted yields and prices at final harvest some months after the interim reporting date. Resulting forecasted values were hypothetical. They could not reflect variations in future balance-date valuations from risks actually experienced due to climatic or disease events on harvested yields, or market supply/demand factors potentially affecting final realised prices for harvested products. Regardless, any non-cash value increment to the vine value was credited as operating 'revenue' in the income statement. Therefore profit recognition was advanced by a subjective and unaudited asset-revaluation process. Moreover, any dividends paid on unrealised profits would not be eligible for franking credits (*ibid.*, p. 55).



Booth and Walker summarised their criticisms that:

- *it is false under the standard to measure vines at their NMV when there is no exit or entry market value for mature grape vines;*
- *it is misleading, and not “faithful representation”, to report profits derived from a vineyard are earned as soon as the root-stock undergoes biological change;*
- *it is misleading to make an artificial distinction between land, non-SGARA vineyard infrastructure and bearer-SGARAs when the elements are interdependent; and*
- *it is misleading to report that all vineyard profit is derived from the vine with none derived from the land or non-SGARA infrastructure (2003, p. 59).*

Taken together, they concluded the SGARA system for Wine Companies ‘*creates a maze more likely to confuse than inform*’ (*ibid.*, p. 52).

#### **6.4.2 Delahunty Trust Report.**

The writer’s project fieldwork occurred in October 2002 and July 2003 (Milne, 2004). This project was commissioned by the Delahunty Trust for the Institute of Chartered Accountants in New Zealand (ICANZ). The objective was to identify experience from practitioners, preparers and users with the SGARA standard preparatory to introduction of the new IAS 41 standard into New Zealand and any recommendations for local preparers, accountants and auditors.

The project pre-dated the AASB’s PIR. However the first visit may have contributed to the AASB initiating its PIR. During his interview, Trevor O’Hoy, CFO for Foster’s Ltd., asked Ruth Picker, as AASB Acting-Chairman, why a survey into experience with AASB 1037 was being conducted from New Zealand, and not by the AASB itself.

Interviews were conducted in New South Wales, Victoria, South Australia and Tasmania, with a follow-up visit to West Australia in July 2003. The interviews reinforced the various Booth and Walker (2003) criticisms outlined above. The full list of interviewees is recorded in Appendix 20.

In summary there were 33 interviewees representing:

- Users:- comprising Banking and Financial Institutional managers, Investment Analysts, Standard & Poors rating specialists and a specialist Financial Journalist;
- Preparers:- with representatives from Wine companies and Forestry entities,<sup>96</sup>
- Auditors:- Partners in the Melbourne head offices of the major firms and field auditors in Tasmania;
- a Government representative from the West Australian Treasury;
- Academics in West Australia and a research student investigating SGARAs in Tasmania and
- an AASB staff member, Angus Thomson.

#### **6.4.2.1. Special Feature Under-Pinning the Agriculture Standard**

One aim of the project was to examine why the SGARA accounting system was developed to include biological transformation as a credit within operating revenue in the income statement rather than a credit to reserves as for any other PP& E revaluation entry.

Two interviewees, a senior Auditor and an Investment Analyst, provided insight from their personal experience at the time. They advised the AARF focus was directed at forestry accounting, virtually to the exclusion of all other SGARAs. The reasons related to the twin dividend declaration and payment criteria under the then Corporations Law:

- **Section 254T** – dividends may only be paid out of profits; and
- **Section 588G** – obligatory solvency test criteria after dividend payment.

Interviewees regarded the legislated ‘profit criterion’ to be a significant contributory element behind AARF’s development of the SGARA Standard, especially for the forestry industry.<sup>97</sup> At the time, there was intended corporatisation of some State Forests and privatisation sales of other forestry plantations. One aim was to facilitate preparation of a prospectus including reported income statement profits and ability to provide profit forecasts and prospective dividend information.

Under prevailing accounting practice any revaluation of forest resources credited to reserves, *i.e.* under the AASB 1010 *Accounting for the Revaluation of Non-Current Assets*, could not subsequently be cycled back to income unless to recognise impairments to

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<sup>96</sup> The principal entities obliged to respond to the AASB 1037 Standard. Field auditors identified special problems for Salmon farmers. These were not elaborated for client confidentiality reasons.

previous valuations. These reserves were therefore not available for dividend distribution purposes when the forest stand was felled at maturity and realised. The *SGARA* standard permitted the future (but not past) accumulated net value from these unrealised biological transformations to be credited directly to operating revenue and therefore eligible for dividend distributions from operating profits, assuming solvency criteria were also met.

The substitution of capital maintenance concepts with the introduction of realised and unrealised fair value and balance sheet accounting principles, for which AASB 1037 was a precedent further confused the situation. The Corporations Law was not amended to provide revised dividend payment criteria when *SGARA* reporting principles were introduced.

#### **6.4.2.2. Role of Australian Accounting Research Foundation Staff**

Many interviewees confirmed the key role of AARF staff as the active principal technical group for agriculture accounting research and standard setting including:-

- the AARF supplied the dedicated research personnel directly or indirectly to consider and formulate an agricultural accounting standard;
- one of the principal AARF staff reporting responsibilities was to the Public Sector Accounting Standards Board ('the PSASB');
- their focus was to obtain comparable reporting bases for the State Governments' and other public entity forestry interests, not only for consistency of reporting but also to aid planned privatisations and sales for which the cycling issue needed to be resolved;
- the AARF sponsored topical research for which, in the context of *SGARA* accounting, the DP 23 Discussion Paper was an important research output; and
- the AARF was responsible for formulating and issuing ED 83; and were incentivised to issue the final AASB 1037 *SGARA* standard before the CLERP-1 became mandatory.

#### **6.4.2.3. Principal Findings**

##### **A. Basis for *SGARA* Standard**

Some interviewees acknowledged from detailed experience the standard was conceived for the Forestry Industry; in particular, to facilitate forestry corporatisation and/or privatisations and to facilitate reporting 'earned' distributable profits.

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<sup>97</sup> As confirmed separately by Angus Thomson, AARF, in November 2002.

### **B. Bearer vs. Consumable SGARAs**

The original DP 23 research was based upon consumable-SGARAs. In interviews the proposition was raised by senior executives and leading Accounting professionals that AASB 1037 ought to be split in two; that is, separate sub-standards for:

- consumable-SGARAs – for which AASB 1037 should be retained; and
- bearer-SGARAs - normal modified-historic cost principles for recording assets and inventories follow the same standards applicable to all other industry sectors. If this were adopted it may be necessary to include additional note disclosures for salient assumptions and valuation methodologies.

The drafting amendments were described as easy to undertake.<sup>98</sup> The advantages of separation were seen as: providing consistency and comparability for standards applicable to other industries, avoiding conflict for integrated companies for accounting treatment of inventories; and especially for the elimination of unrealised profits on intra-group consolidation.

### **C. Parallels for Bearer-SGARAs with Other IFRS Accounting Standards**

Interviewees noted that AASB 1037 fair value accounting was claimed to be a logical extension of existing standards for financial instruments, the insurance industry and for investment properties. However they also identified that in Australia those industries have ready and reasonably available continuous price discovery from active and liquid markets. That may be the case too for short term consumable-SGARAs; but not for bearer- and long-term consumable-SGARAs. None were traded in the normal course of business; all were held to maturity. They were formerly subject to modified-historic cost valuations allowing for normal depreciation and/or impairment rules.

On the other hand, for the financial industry, financial and insurance assets held for trading purposes were marked-to-market. Term financial assets were accounted at cost, if held to maturity and met requisite designation criteria with carrying value increments/decrements recorded in reserves. This option was not available for bearer-SGARAs.

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<sup>98</sup> Over two years ago the Malaysian Accounting Standards Board prepared draft standards for the IASB 'inside access' National Standard Setters (NSS) group, comprising some fifty members from 27 jurisdictions (including Canada and the FASB) and 10-15 members from the IASB and IPSAS. The MASB proposal is to separate 'Consumables' (retain in IAS 41) from 'Bearers' (to IAS 16).

**D. Practical Problems in Applying AASB 1037**

There were concerns expressed by Preparers, Auditors and Analysts about practical operation of the standard. These included potential double- or multiple-counting of revenues; unwarranted reporting of unrealised and potentially inflated or fluctuating revenues and profits; the requirement to undertake SGARA valuation entries for published interim accounts; artificiality of determining bearer-SGARA asset values-by-deduction and inconsistent recognition of unrealised inventory/asset price movements as revenue, rather than transfers to then cycling from reserves on realisation.

**E. Doubts about Active and Liquid Markets being Available**

Interviewees highlighted that the AASB 1037 standard, and all the discussion surrounding its development, assumed that SGARA asset values would be derived from active and liquid markets. However, for virtually all reporting entities, SGARA asset values were determined in-house using the surrogate NPV calculations.<sup>99</sup> As a result the stated objectives for developing AASB 1037 to achieve comparability and reliability could not occur in practice – unless all valuation assumptions and methodologies were identical and technically consistent for all reporting entities.

**F. Users' Views on the AASB 1037 Standard**

None of the Banking, Analyst or Rating Agency user interviewees subscribed to the view espoused by the AASB, and IASB, when referring to the *SGARA/Agriculture* standards, that standardised financial reporting based on suspect non-realisation-based asset values or reported profits would assist companies to raise capital globally. This notion was described as bizarre. Rather, these parties relied on other cash-based metrics for their analyses and forecasting models – or they seek, and obtain, special purpose specific information and reports, under confidentiality, not normally available to shareholders or other users under ASX continuous disclosure rules.

In their opinion, SGARA-type information was the antithesis of what fair value financial statements should report. They claimed it inconceivable that inflated, unrealised profits stemming from adherence to AASB 1037 rules represented sound reporting bases given (then) corporate excesses in local and international markets.

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<sup>99</sup> Confirmed independently by Herbohn K.F *et al.* (1998) and Dowling and Godfrey (2001).

### **G. Interviewees Recommendations for New Zealand**

Interviewees recommended that given the relative importance of the agricultural sector in New Zealand, local standard setters should ensure an education programme be established for the standard before it became effective for the benefit of preparers, practitioners and users alike. This had been lacking in Australia, although originally promised by the AASB.

### **6.5 Subsequent Academic Surveys**

Two recent surveys have sought to determine whether the original standard-setter objectives to obtain consistent, reliable and comparable accounting by agricultural entities have been achieved in Australia, and in a broader international context covering France, Australia and the U.K. Their *ex post* conclusions corroborate some of the findings in this study on expectations made in submissions on the standards, and in the Field Test and PIR.

#### **6.5.1. Survey in Australia by Williams and Wilmshurst (2008)**

The questionnaire survey sought to identify the types of measurement methods used for wine industry and forestry participants for their SGARAs (AASB 1037), or proposed for biological assets (AASB 141). The results found consistency in measurement valuation methods has not been achieved. However they did indicate a relative consistency of use of seven different measurement methods, including in one instance five different methods by one entity for one SGARA. Consistency in practice through time did allow a degree of comparability for an individual entity, but not for financial results for a sector.

#### **6.5.2. Empirical Investigation of IAS 41 Practice in France, Australia and the U.K.**

This survey by Elad and Herbohn (2011) confirmed *inter alia* that '*there has been strong opposition to IAS 41 in the plantation and forestry sectors...[and] systematic national differences in accounting policy choices...not only by companies, but also by auditors and regulators*' (p. viii). They also found '*a high level of agreement the costs of measuring and reporting biological assets outweigh the benefits*' (p. x). Thus '*the IASB [should] revisit the standard not only because it has failed to change farm accounting practice but also creates the illusion of comparability despite the range of options allowed under the standard*' (p. x). A principal conclusion was that '*IAS 41 has*

*failed to foster the international comparability of accounting practices in the agricultural sector'* (p. 123).

## **6.6 Concluding Comments**

The AASB's PIR proved to be a reality-check on the concerns and issues Preparers, Auditors and Users were experiencing with the AASB 1037 standard.

Accounting standards setting contains many of the desirable post-enactment review characteristics, found for example in engineering and business projects. This is the only PER that has been found - although there may have been others as comprehensive, but still unreported. However the IASB has stated its intention to FASB to issue PIRs. The first is for the IAS 14 *Segment Reporting* standard in 2011. This was also indicated as a review item in Sir David Tweedie's presentation slide No. 27, referred to in [Section 5.5](#) above.

In the circumstances, and given the steadfast defence of *SGARA* accounting, the AASB's PIR, and its principal recommendation, it is regrettable it saw fit not to publish the outcome of its survey for benefit of contributors, the profession, for standard setters and, more generally, for examination by preparers, the academic community and other users.

Although standard setting for the *SGARA/Agriculture* standards notionally followed a *mobilisation* consultation model, lack of any report-back on the AASB's PIR reflected poorly upon the transparency of rule-making processes undertaken by the AASB and IASB gatekeepers. It appeared that key insiders undertook virtually all preparatory work internally through to eventual decision-making. This reflected elements of the Cobb *et al.* (1976) *inside access* model and some of the related Mitnick (1980) gatekeeper archetypes. It was inevitable the standard was controversial and that it received the criticisms it did.

There was little responsiveness to or policy-oriented learning from respondents' constructive recommendations, particularly through the final exposure draft rule-making stage, the PIR, and from academic commentaries, as might be anticipated under an *Advocacy Coalition Framework* (Sabatier and Jenkins-Smith, 1993).

## Section 7. CONCLUSION

Financial reporting for agriculture entered the formal agendas of the Australian and International standard-setting bodies during the 1990s. This study has examined the political processes and the role of the ‘key players’ in the development and issue of separate *Agriculture* standards in Australia and by the IASC, followed by events during and after transfer of IAS 41 to Australia and New Zealand.

The study considered in depth the inter-play between two separate activities:

- technical accounting rules devised for an omnibus standard for all agricultural activities relative to past generally accepted sector accounting practice; and
- political processes by which the gatekeepers, namely, the key staff, technical advisers and decision-makers, developed then decided upon the new standards, and their inter-agency relationships.

The standards were controversial.

The new technical accounting rules made little commercial sense to many listed agricultural entities. For some, the standards required potential multiple-revenue reporting for the same income stream, advanced profit recognition at harvest many years prior to eventual product realisation, revenue valuation of assessed changes in integrated asset values independent of the *terroir* in which they co-exist; and, inconsistent treatments for accounting and reporting of agricultural activities compared to inventories and assets in contemporary accounting standards. Accordingly, extensive lobbying representations were undertaken by preparers, academics and others.

The study examined the technical, political and controversial issues in terms of regulation of accounting rule-making processes by considering the following research questions:

- why and how the AASB’s *SGARA* and IASC’s *Agriculture* topics gained access in respective regulatory agencies;
- how each topic progressed through each of the respective rule-making stages;
- who were the key insider gatekeepers controlling respective agendas; and
- how respondents reacted to the proposals, and the gatekeepers’ responsiveness.



## **7.1 Research Questions and General Findings**

### **7.1.1 Why and how the agriculture topics gained agenda access and entrance**

In the late-1980s, there was potential to consider new accounting rules for agriculture. Other accounting standards specifically excluded forests, livestock and other regenerative natural resources from their ambit. But this was insufficient *per se* for the topic to enter the agenda of standard-setting agencies.

The two standards had disparate beginnings. In Australia, Angus Thomson at the AARF confirmed that impetus to propel the topic onto the regulatory agenda came from State Government pressures to facilitate forestry corporatisation and privatisations. By the time Don Roberts at the University of New England enquired about relevant accounting practice for forestry and livestock, the reply from Ms Curran, AARF Technical Director, in May 1989, confirmed agenda access had occurred. A project was already authorised. An objective was to be able to accrue revenues from specified agricultural activities from which dividends could later be paid under the then Corporations Law. In short, without public controversy suggesting there was a problem in existing practice, the topic was promoted by the accounting profession's AARF, including the PSASB, as a topic also to be addressed by the Commonwealth's standard-setting agency, the AASB.

The IASC was then pursuing a comprehensive global standard-setting objective initially to obtain recognition of its Core Standards by IOSCO for acceptance by the SEC. From the late-1980s, ECSAFA and the ASEAN country groupings were actively considering development of an agriculture accounting topic, amongst others. The IASC decided to take over these topics, albeit with some reluctance, rather than allowing competing trans-national standard setting to develop. Issue creation was triggered, and facilitated, when the World Bank offered the IASC's Secretary-General, David Cairns, a significant grant in 1994 to fund development of an issue relevant for its Developing and Newly-Industrialising Country clients. The discussion focussed on agriculture. Agenda entrance occurred and was approved by the Board in June 1994. Staff and a specially appointed Steering Committee were required to present a specific project *Point Outline* to the Board in March 1996. Once approved, the Board formally authorised work to begin on a 'Draft Statement of Principles for *Agriculture*'.

### 7.1.2. How each topic progressed through each of the respective rule-making stages

Each project followed equivalent rule-making stages. These are summarised above in terms of a framework proposed by Walker and Robinson (1993), itself adapted from the Cobb and Elder's (1972, 1983) agenda-building processes description. The IASC Board formally endorsed its internal rule-making deliberation processes during 1992-1993. This was consistent with that framework with one exception; it excluded allowance for a formal post-enactment review (PER) stage. [Section 4](#) described the progress of each topic through respective AARF/AASB and IASC internal processes. [Section 5](#) examined subsequent developments in Australia and New Zealand as IAS 41 transferred to these domains.

An unexpected benefit of the agenda-building framework was identification of a formal PER stage as validation of rule-making processes (Cobb and Elder, 1983; Walker and Robinson, 1993). A PER is rarely undertaken; or, if so, reported. However, as discussed in [Section 6](#), a post implementation review was undertaken for the AASB's *SGARA* standard; but not made public. There was no evidence reported by the IASB, or in Australia in the formal FRC/AASB Annual Reports that a PIR was contemplated, or completed. The only reference found was when the NZ Financial Reporting Standards Board was finalising its NZ IAS 41 standard.

A feature of these rule-making phases for *Agriculture*, followed by both agencies, was that they were predominantly inwards-focussed. They were consistent with the Cobb, Ross and Ross (1976) *inside access* model, rather than the *mobilisation* model, which would have envisaged prior support from external constituencies, or the *outside initiative* model stemming from an accounting crisis or misleading financial reporting.

In Australia, the original AARF *Project Brief* was pre-occupied with biological growth and re-generation, particularly for forestry and livestock. This overlooked their monetised attributes. Furthermore, the basic biological distinction between the bearer- and consumable-agricultural sectors developed over many decades was subordinated. An omnibus standard conceived on a flawed premise that forestry and livestock, as 'consumables', represented all SGARAs was problematic, and the result controversial.

At the IASC level, E65 respondents submitted the conceptual framework then under development was insufficiently advanced. The proposed standard did not allow for the historical role of the income statement to measure an entity's realised operational and financial performance, or dividend-paying capacity. Instead, it measured unrealised mark-to-model fair value changes in balance sheet asset values as revenues within the income statement, without differentiation between realised income and unrealised changing balance sheet inventory and asset values. Inconsistent asset and inventory valuation methodologies were proposed for agriculture compared to other industries and other contemporary standards. No attempt was made to reconcile these objections or conform valuation and reporting treatments. Little attention was paid to industry and professional accountants' experience and academic submissions. These resources went untapped.

The study also uncovered reports not issued publicly by the IASB or AASB standard setters. The most significant were the confidential FTP and PIR survey reports. They are recorded in full in [Appendices 15, 21 and 22](#) respectively as contributions to the literature.

The purpose of the IASC Field Test in 2000 was to gauge the acceptability of the E65 proposal. The results were not published. The Field Test findings demonstrated rule-making design may require reconsideration as a process priority. It should have preceded exposure draft issue, as a draft proposal, rather than being conducted afterwards. IASC rules did envisage more than one exposure draft may be necessary. This would have been the opportunity to address the many critical submissions from both E65 and the Field Test. Instead, the report was confidential, and remains so. Further consideration was too late as the topic was overtaken by the IASC's dis-establishment timetable.

The principal recommendation from the AASB's PIR, reported to the IASB Chairman in November 2003, was to separate bearer-SGARAs, in particular wine companies, from IAS 41 before the IAS 41 formal commencement date in 2005. The IASB has ignored this recommendation to date.

Another feature of rule-making stages discussed in the study was that active inter-agency lobbying replaced customary inter-agency co-operation. AASB representatives lobbied direct for changes to the IASC's DSOP and E65 in support of accounting concepts

contained in the AASB 1037 *SGARA* standard. The apparent objective was to lead and influence IASC Board deliberations as a pre-emptive strategy to achieve local ends. These were firstly, to complete local AASB 1037 approval before the local CLERP-1 legislation became operative; and secondly, to lobby the IASC to adopt the approved Australian standard as its own in order to vindicate AARF/AASB initiatives to domestic critics.

This added an extra dimension to the changed status of national standard setters. They were in the process of becoming client standard takers but retained power and inclination to lobby in their own right. Some examples of inter-agency lobbying are quoted elsewhere in the literature. These include interaction between the Australian Government and the accounting profession Walker (1992); between Australian government agencies and a standard-setting agency with conflict between Australian public- and private-sector agencies (Walker and Robinson, 1994), and equivalent interactions between the FASB and the U.S.A.'s SEC (Walker and Robinson, 1993).

Finally, there was evidence the Agriculture proposals promoted by the key staff insiders did not have full support of all IASC Board voting delegates. The standard was the only one in the IASC's history to achieve approval by the barest possible two-thirds majority for the E65 exposure draft, and three-quarters majority for the IAS 41 standard – and then only after late political compromise, at Board insistence, permitting historic cost as part of the fair value hierarchy in certain circumstances. That over-ruled the SC recommendation. Collectively voting delegates appeared to lack conviction that the proposal was of an acceptable quality. Another concern highlighted by Camfferman and Zeff (2007) was that approval of this minor standard might create precedents for succeeding standards.

### **7.1.3. Who were the key insider gatekeepers controlling respective agendas**

In Australia, Warren McGregor was the AARF Executive director on behalf of the AARF/PSASB/AASB Boards with Robert Keys and Angus Thomson in key AARF technical support and development roles. Ian Mackintosh as Director of the PSASB was another insider at the time.

Within the IASC, the principal exposure draft promoter was Paul Pacter as the IASC's International Accounting Fellow and Project Manager for the *Agriculture* SC for about 18 months until he retired from the IASC in June 2000. He was replaced by Rieko Yanou. Others included Ian Kirton, the original SC Project Manager and other SC members during its seven year history. SC members are recorded in [Appendix 8B](#). Liesel Knorr was the IASC's Technical Director until late-1999. No reference was found in the literature to any comments on the Agriculture project by her replacement, James Saloman. He was the IASC's Technical Director until eventual IAS 41 approval in December 2000.

A key link between the two agencies was Warren McGregor who, in addition to his AARF responsibility, was a long-standing Technical Adviser to the IASC Board including the period the Agriculture project was developed from the mid-1990s. He retired from the IASC during 1999. Camfferman and Zeff identified other '*Australian champions*' involved in IASC activities. Amongst these was Kenneth Spencer, AASB Chairman during the exposure draft and promulgation stages. He co-signed the AARF submission on E65 with Ian Mackintosh, and he led the campaign to obtain IASC approval for IAS 41 similar to the already-approved AASB 1037 *SGARA* standard.

They were the key gatekeepers for the AARF's *SGARA* and IASC *Agriculture* Projects.

A feature of rule-making processes, at least initially, was evidence of co-operation between the AARF/AASB and IASC insider technical advisory staff. Warren McGregor would have been a key intermediary. However, that stance and inter-agency strategy changed in mid-1997, following completion of the AARF's RIRDC research project which crystallised proposals for *SGARA* accounting. This was manifest in the AARF's submission on the IASC's Draft Statement of Principles in May 1997, following which the AASB accelerated issue of its ED 83 exposure draft and the AASB 1037 *SGARA* standard as the basis for lobbying on the final IASC processes.

Some IASC members, technical adviser delegates and other insiders appeared to play activist roles. In total, there were 60 submissions on E65. Ten were signed by individual Board voting or Technical Advisory delegates. [Appendix 8A](#) identifies those signatories. There were five signatories from Board members in country voting delegations and five

from the Technical Adviser categories. One Board member and five Technical Adviser signatories were not fully in support of approving IAS 41 as submitted.

Such potential conflict of interest may not have been identified previously where decision makers may serve as ‘players’ and as ‘umpires’. Whilst it might be appropriate for insiders to express and formally record their preliminary views during draft rule-making stages – it raises a question about the robustness of governance procedure and integrity of voting process observed at the final decision-making stage. Minutes were not available which recorded the individual member from each country delegation who was formally permitted to vote (or abstain) their approval to the IAS 41 standard. Camfferman and Zeff referred only to country voting delegations.

#### **7.1.4 How respondents reacted to the proposals, and the gatekeepers’ responsiveness**

Findings from the study confirmed evidence of a disregard for substantive submissions from practitioners, regulatory agencies and industry representatives. Standard-setting processes envisage consultation with users for legitimacy and user acceptance. The claimed beneficiaries of these processes, the users of financial reports, as opposed to the users of accounting standards, became ever more remote and lobbyists’ concerns even less recognised. When users were invited to participate, the standard was virtually in final form. Few users participated. Those who did were critical. Their contributions were too late and were overlooked or denied without reconciliation or validation. The process proved to be insufficient and unresponsive. Instead, *inside access* rule-making processes were driven by internal needs or preferences, and timetables.

The case study methodology also found that lobbying at the early stages of IASC agenda development was mainly confined to other regulators, standard setters and the profession.

By the time exposure drafts were released, gatekeepers’ intellectual and conceptual capital was too far advanced to reconsider past decisions and to allow alternative interpretation or admit incongruence - unless insisted upon at Board level. In the case of the IASC’s *Agriculture* standard, failure nearly occurred at that final stage. It was only overcome by necessity, and political compromise, not by conceptual design.

Table 33 lists the respondent categories across each of the IASC, AASB and New Zealand rule-making stages:

***Table 33. Respondent Categories on Each Agriculture Standard Rule-Making Stage***

<b><u>IASC</u></b>	<b>Total</b>	<b>Regulators; Standard-setters, Professional Bodies</b>	<b>Agricultural Entities &amp; Ag. Bodies</b>	<b>Other Users &amp; Others</b>	<b>Academics</b>
<b>DSOP</b>	<b>42</b>	<b>26</b>	<b>6</b>	<b>7</b>	<b>3</b>
<b>E65</b>	<b>60</b>	<b>38</b>	<b>8</b>	<b>9</b>	<b>5</b>
<b>Field Test</b>	<b>28</b>		<b>28</b>		
<b><u>Australia</u></b>					
<b>DP 23</b>	<b>4</b>		<b>4</b>		
<b>ED 83</b>	<b>46</b>	<b>16</b>	<b>22</b>	<b>4</b>	<b>4</b>
<b>ED 114</b>	<b>20</b>	<b>9</b>	<b>5</b>	<b>3</b>	<b>3</b>
<b>PIR</b>	<b>26</b>	<b>6</b>	<b>16</b>	<b>2</b>	<b>2</b>
<b><u>New Zealand</u></b>					
<b>ED-90</b>	<b>100</b>	<b>57</b>	<b>34</b>	<b>6</b>	<b>3</b>
<b>TOTAL</b>	<b>326</b>	<b>152</b>	<b>123</b>	<b>31</b>	<b>20</b>

One finding is the preponderance of submissions at the international level by regulatory bodies, standard-setters and professional accountants, including auditors. Also, at that level, few responses were made by affected agricultural entities. Camfferman and Zeff commented on this. Lack of responsiveness contributed to the IASC Board's decision to initiate the Field Test Project prior to final consideration of the IAS 41 standard. In addition, there was determined lobbying against the E65 proposals from the profession, standard setting bodies, academics and some IASC delegations.

The converse applied when requests for submissions occurred at the national level. There was lack of support, and lobbying for change, in submissions by Institute Branches (New Zealand) and by professional bodies, auditors and chartered accountants across Australasia. There were significantly increased submissions from agricultural entities at the exposure draft rule-making stage.

These findings were contrary to expectations from Young (1994) that later stages are least contested. Instead, as suggested by Sutton (1984), and Young (1994), the findings confirmed lobbying by preparers will occur individually or collectively when their economic interests risk being adversely affected.

Evidence from the Exposure Draft representations, the IASC Field Test Report, and from the AASB's PIR survey report and recommendations revealed, in answer to the Howieson (2009) question, a general lack of responsiveness to submissions by respective standard setters. This reflected the prevalence of gatekeepers' *inside access* practice (Cobb *et al.*, 1976). There was no responsiveness to Field Test representations or by the IASB to recommendations made by the AASB following its PIR. The report and recommendations for change were not published. Moreover, once IAS 41 *Agriculture* transferred to the local Australian and New Zealand domains there was no scope materially to alter the approved international standard – except by reference back to IFRIC for guidance or interpretation, or to the IASB itself. There was only one material amendment permitted eight years later to correct an obvious error in the original standard.

The analysis also revealed a missing link not referenced elsewhere. Most principles for reporting agricultural activities were well known and understood historically. The proposals were capable of resolution by or with advice from experienced preparers, users and independent academic accounting commentators. These resources went untapped.

The application of the fair value concept for Agriculture was inconsistent when compared to other standards. Submissions showed the proposed standard would not be accepted by many respondents, unless specific concerns were addressed, including a practical Field Test and education programme to validate the new proposals. The former was completed, but not reflected in the standard. As a result, internal gatekeeper processes exposed reporting entities and investors to new financial reporting and governance risks not encountered by other industries responding to other contemporary standards.

The reliability of changes in asset carrying values reported as unrealised revenues in the income statement was subject to significant risks and uncertainties. There were risks of subsequent climatic or disease events and uncertainties about forecast maturation



capability, each potentially impairing realised quality and yield at harvest or sale. Furthermore, the effects on reported profits conventionally liable to taxation, or available to determine distributable net income for dividend payment decisions, were significant with unintended consequences. Pro-cyclical effects either exacerbated over-stated asset and inventory values and therefore profits or, in the converse, placed pressures on borrowing covenants and viability. No other industrial reporting entities faced this situation to that degree. As a result the standards were controversial, and remain so.

A decade later there are now fewer listed Australasian entities engaged in agriculture. Intervening adverse trade cycles would be one reason. However, arguably, unintended consequences were delisting of former listed entities and takeovers by overseas non-IFRS reporting entities. They were then no longer required to report under the standard.

#### **7.1.5 General Summary**

In overview, the development of the *Agriculture* standards revealed an incomplete, introspective and unresponsive process by the key insider players, the gatekeepers, throughout all rule-making regulatory stages in respective Australian and IASC domains.

##### **A. An Incomplete Process**

Initial work in Australia specified in the *AARF Project Brief* to its UNE contractor pre-determined the eventual output. The focus was upon forestry and livestock - both 'consumable SGARAs' in the UNE taxonomy. Extrapolation from these specific sectors to an omnibus standard encompassing bearer-SGARAs was simply identified as subject to confirmation by further research. If undertaken, which is unlikely, it was never reported. As a result, and given the profound biological differences, the assumed commonality of net fair value measurement accounting treatment for bearer- and consumable-SGARAs in the eventual standard was likely to be controversial. In particular, whilst market prices were readily available for some, *e.g.* livestock, there were none on an interim basis for others, *e.g.* for vines; and for forestry, surrogate valuation measurement was necessary by net DCF determination. This ensured a loss of reported income comparability between entities because of differing internal growth, price, cost and discount rate assumptions.

The Australian DP 23 and the IASC's DSOP maintained a common link with the past in separating accounting treatment of SGARA physical volume or quantity changes from price changes. It proposed that the monetary attribution of physical change be recorded in the income statement to reflect operational performance, represented by biological transformation for natural increase, maturation and death, as well as from sales. Change attributable to varying asset prices was to be recorded after operational performance, more commonly in reserves within equity. The latter was the equivalent to modified-historic cost revaluation accounting treatment in PP&E standards.

The material change, unique to *Agriculture*, was developed from the RIRDC-sponsored research undertaken by AARF insiders. This concluded initial recognition of all biological assets and inventory, together with periodic changes in balance sheet values, should be recorded at net market value as a combined physical and value revenue item in the income statement, applicable to all agricultural activity, designed for Australian conditions.

The AARF/AASB then lobbied actively with their IASC counter-parts to adopt *SGARA* accounting for the IASC *Agriculture* project. This was not backed by field research by the IASC's SC to confirm applicability to differing agricultural practice in developing countries, the original target for World Bank project funding, or for acceptability for intensive north-west European agricultural systems or North American practice.

The result was submissions initially by various national standard setters confirming agriculture should no longer be excluded from mainstream IASC standards. However there was other lobbying by standard setters, practitioners and auditors, preparers and academics. The tenor was that insufficient research was undertaken into the implications of discarding historic cost entirely; the inappropriateness of harvest-based value for some SGARAs where further processing was necessary, to ensure marketability and resulting value determination; the unique effects of anticipating unrealised profits on inventory recognition at net market value, instead of addressing the *Inventory* standard itself; effects on fiscal and dividend determination; and, completion of concurrent projects on the conceptual framework for valuation measurement and on the G4+1 comprehensive income statement work. The IASC's Field Test should have helped resolve many of these issues. It was a limited exercise conducted too late for incorporation into the IAS 41 standard.

### **B. An Introspective Process**

The rule-making model process formally defined by the IASC was a template also used in principle by other standard setters. This elaborated the systematic internal agenda processes to be agreed and undertaken by staff also with adequately resourced steering committees, reporting for timely Board deliberations within defined timetables. The expectation was that standards would, as a result, be well considered during respective agenda stages. Requisite wide-spread acceptability should occur progressively following consultation with and endorsement by constituent members and users generally. This process reflected the Cobb, Ross and Ross (1976) *mobilisation* model. However, it risked endorsement occurring too late in the rule-making process to be effective relative to intensive work and internal lobbying amongst key staff insiders and with Board members.

For Agriculture, although notionally following the above, the prevailing process across the Australian, International and, ultimately, New Zealand domains reflected instead the Cobb *et al*, *inside initiative* or *inside access* models. The former was demonstrated by the activities of issue entrepreneurs (Cobb and Elder, 1983); for example, the AARF research initiative to develop and promote the SGARA accounting system itself. Subsequently that initiative was transferred through specific inter-agency lobbying strategies with IASC Board delegates, steering committee and staff insiders by the ‘Australian Champions’, aided also by supportive key IASC staff.

The *inside access* introspective processes were manifest in a number of ways. These included: internal consideration of and defence against adverse submissions in each of the three standard-setting domains; suppression of the IASC’s Field Test Report and results of the AASB’s confidential PIR survey, together with eventual survey recommendations to the IASB Chairman.

### **C. An Unresponsive Process**

A feature of the study was the lack of comprehensive engagement with respondents to overcome adverse submissions, in particular at the Exposure Draft stage in each domain. There had been ample evidence of potential difficulties raised in submissions from standard setter agencies; from preparers – especially bearer-SGARA reporting entities; from the profession and auditors, and from academic submissions and journal articles.

The staff supplementary, non-officially authorised, 'Bases for Conclusions' attached to the AASB 1037 and IAS 41 standards respectively only partially addressed concerns. The outcome of both the Field Test and PIR surveys did not result in change to the final standards. One stated purpose of the AASB's PIR was to recommend changes from experience prior to the IAS 41 implementation date in 2005. The IASB rejected the principal recommendations. They remain unaddressed. However, Sir David Tweedie did confirm in 2010, a decade after IAS 41 issue, that the Agriculture standard was one of nine standards requiring full reconsideration - when IASB agenda priority permits.

The reference to IFRIC for a simple correction to the measurement error in IAS 41:21 was finally amended by the IASB eight years after IAS 41 promulgation; in the meantime, the clause was effectively ignored as an unworkable irrelevancy by preparers and auditors.

## **7.2 Research Methodology**

A case study was the most appropriate methodology to research the 'how', 'who' and 'why' questions above (Yin, 2003). The study utilised the Cobb and Elder (1983) and Cobb *et al.* (1976) agenda concepts. It demonstrated the usefulness of the framework, summarised by Walker and Robinson (1993), for investigating two chronological rule-making processes phased across the Australian, International and New Zealand domains. Gatekeepers were shown to play key roles in these regulatory processes.

The ideas and information espoused in the following principal references on regulation and related background technical and lobbying issues were invaluable: Cobb and Elder (1983) and Kingdon (1995) on agenda-building processes, power and politics; Cobb *et al.* (1976) on institutional dynamics; Mitnick (1980) on gatekeeper archetypes and regulatory issues; explanatory overviews of rule-making process development *e.g.* by Beresford (1988; 1993), Walker and Robinson (1993), and Young (1994); and, lobbying rationale, processes and practices described, *inter alia*, by Sutton (1984), Walker and Robinson (1993), and Young (2003). Finally the opportunities identified by Sabatier and Jenkins-Smith (1993) for policy learning processes potentially available but not seized upon to benefit development of standard-setting for this topic.

In overview, the case study research reported in this study went beyond the conventional approach described in the literature of examining the content of more than 300 written submissions worldwide and interpreting the ‘votes’ for, or claims against, the proposals being considered. Whilst necessary, it proved insufficient. Earlier studies do not adequately identify the extent to which gatekeepers can interact to influence board deliberations on technical accounting rules. Moreover, past studies have tended to focus upon a single country or single regulatory agency. The advent of the IASC, now IASB, has altered regulatory arrangements. This was a new domain offering different scope for internal and external lobbying. The study provided evidence about technical, political and transfer processes across the Australian, IASC, New Zealand and IFRIC domains and how their aims became inter-twined when subject to intra- and inter-agency lobbying.

Evidence was also obtained from a variety of other sources, *e.g.* study of accounting methods and reporting in annual reports, preliminary interviews with practitioners, analyst and banking users, with preparers, and with a key technical adviser, Angus Thomson, in the SGARA-development process. Investigations sought and reviewed a range of ancillary material for each rule-making stage with a focus on the role of the gatekeepers. Some were published *e.g.* the Camffermann and Zeff (2007) IASC history and IASC and AARF staff commentaries as the topic matured. But some were unpublished as previously described.

### **7.3 Other Insights**

#### **7.3.1 Changed Lobbying basis for International Accounting Standards**

As standard setting moved into the international domain, lobbying activity has changed. Instead of lobbying *ex ante* as rule-making processes mature, this study showed lobbying intensified at the final exposure draft stage, and afterwards. There are a number of possible reasons. The IASC/IASB process has become more remote and specialised with increased control by insiders. There is a continuous stream of new drafts, guidelines, amendments and standards so that only a few technical specialists can keep up-to-date with all current developments. One important consequence is that unless significant adverse economic effects are readily apparent, fewer submissions are supplied from practical experience by preparers, users or academics. Therefore *ex ante* lobbying becomes less effective as a formal process. If it occurs at all, preparers are more likely to lobby *ex post* reinforced by

actual experience. This suggests a formal post-enactment review process should become an essential rule-making validation phase.

Hitherto, the literature has focussed on lobbying on national standards in a national domain; or, for international standards applied globally. This study examined the phased processes across the two original standard-setting domains. For *Agriculture*, there were very few submissions initially from preparers, or users worldwide. Their lobbying effort occurred too late when different, significant proposed changes to accounting and reporting practices occurred in the exposure draft compared with the original AASB and IASC draft statements of principles. These changes altered the proposed standard materially. Each was developed by ‘insiders’. This effect may have been confined to this standard, or may reflect a wider phenomenon. Whichever, determined *ex post* lobbying by preparers was one reason the AASB justified their post implementation review, with IASB support. The result was the significant AASB recommendation to the IASB that IAS 41 be split in two.

### 7.3.2 Is the Agriculture Standard Really Necessary?

Up until the late-1990s, accounting and reporting for agricultural activities was specifically excluded from other relevant standards. The original AARF *Project Brief* shaped the content of the DP 23 *SGARA* paper developed by contractors at the University of New England. DP 23 defined biological generation and re-generation characteristics for forestry and livestock. The possibility that definition of an issue might delimit alternatives was identified by Cobb and Elder (1983). When pursuing the AARF’s contract brief, the UNE contractor was constrained in devising a taxonomy defining biological SGARAs. The continued concentration on the living aspects of SGARAs overlooked monetary attribution of asset values for accounting purposes, as occurs for all other tangible assets.

In effect, and as identified in DP 23, a consumable-SGARA is an inventory item. Its cost, value and volume increases just like any physical widget until it eventually reaches marketable-product status. In some cases, the consumable is a short term crop – which the standard setters later acknowledged should not necessarily respond to the *Agriculture* fair value model. In other cases, *e.g.* a tree, the consumable is, in practical terms, a long term inventory item with similar maturation periods to some *produce* of bearer-assets, *e.g.* a top vintage wine, brandy or whisky. Respondents recommended that before the agriculture

standard was confirmed, the IAS 2 *Inventory* standard be reviewed to eliminate existing exclusions for biological inventories; such that all inventories become accounted consistently on recognition at lower of cost or market value to avoid reporting unrealised profits for agricultural products at net market value.

Similarly, other submissions, notably by Keith Alfredson, and also the AASB PIR letter to the IASB Chairman, recommended bearer biological assets should be excluded from the IAS 41 standard for reliability reasons. Instead, they should be accounted under the IAS 16 *Property, Plant and Equipment* standard. Moreover other anomalies were identified by academic commentators (*e.g.*, Priest, 1997; Amen, 2000; Clark *et al.*, 2002; Booth and Walker, 2003) where, for accounting purposes, the standard deemed bearer-assets viable when physically separated from agricultural land. Pastoral grass attached to land was not considered a reportable biological asset. Other assets integral to and supporting biological asset economic and physical viability, *e.g.* tradeable quotas, licences and water-rights, were treated as Intangibles under IAS 38 on a completely different accounting basis.

Standard-setter, professional, and preparer submissions on E65 recommended priority be given to performance measurement and comprehensive income projects then under G4+1 consideration. The purpose was to consider reliable and relevant treatment of realised operational results *vs.* unrealised balance sheet changes in carrying values where both were recorded as revenues in the income statement. Respondents sought all value changes for all assets be treated consistently within comprehensive income, with cycling permitted on realisation from reserves to operating income for consistent operational performance.

Taken together, if implemented, the need for a unique *Agriculture* standard could be subsumed into existing revenue, asset, inventory and presentational standards; albeit with enhanced disclosures appropriate for biological asset measurement and valuation bases.

#### **7.4 Possible Areas for Future Research**

An immediate question arises as a result of research study findings: was the experience of this standard an aberrant example, or symptomatic of systemic weakness in standard-setting processes?

The processes in Australia, and for the IASC, were necessary - but not sufficient - to produce a high quality, transparent and consistent accounting standard. Vital supporting information was not released publicly to users. The underlying political and insider processes themselves warrant reconsideration to minimise future repetition. For example, were, or are, voting processes influenced in the same way for other standards by interested voting delegates, or technical delegates, with associated governance implications.

Other research possibilities include:

**7.4.1.** to examine using a case study methodology the political processes under-pinning any of the standards identified by Sir David Tweedie as being '*conceptually incorrect or in need of overhaul*' and the reasons for this statement, as learning for the future. Examples include IAS 12 *Income Taxes*, IAS 38 *Intangibles*, IAS 39 *Financial Instruments*, and IAS 40 *Investment Properties*. In view of the significance to agricultural preparers worldwide, the 'agriculture' component of the *Small and Medium-sized Entities* standard may warrant examination pending its adoption, or otherwise, in Australia and New Zealand.

**7.4.2.** to help determine consistent application across a number of existing standards, as identified (in para. 7.3.2) above. 'Fair value' measurements derived from market prices for biological assets and produce were presumed, by definition, to be readily available from active and liquid markets. Prior history and many submissions showed this not to be true except for short-term readily-saleable agricultural produce and livestock. Price discovery information in *financial* markets is usually readily available and visible – but this is rarely the case for other *asset* markets as was demonstrated by findings of extensive use of surrogates, mark-to-model reporting and, in some circumstances, use of historic cost for accounting under the standard.



Translation of individually fair-valued balance sheet assets was then applied inconsistently and non-comparably with other standards. Except for impairments, changes in values for *financial* assets held-to-maturity are retained in reserves, changes in *intangible* asset values are only permitted in limited and specific circumstances, whereas changes in assessed carrying values for *agricultural* assets are reported in full as unrealised revenue in the income statement, as is the initial recognition of inventories at harvest, causing premature, even hypothetical, profit recognition and anomalies for subsidiary consolidations. Present proposals do not permit cycling transfers from reserves, or within comprehensive income, on actual realisations from revalued asset values held in reserves. Numerous submissions recommended this occur to meet practical and legislative requirements – but no rationale was supplied to reject those representations.

Further academic research could identify consistent parameters for a full fair-value attribute basis for the balance-sheet-oriented approach based on fair value measurement, within the conceptual framework, as it applies in principle for Agriculture under IAS 41. This would envisage consideration of the purpose of the income statement, presentation of operational financial performance, including earnings-per-share, and the appropriate recording of internally-derived surrogate valuations or previously unrealised assessed values upon realisation, reconcilable with the statement of cashflows.

**7.4.3.** to investigate the role of auditors and securities regulators as *de jure* gatekeepers with enforcement powers, equivalent to those responsible for formulating accounting standards, when auditing or reviewing audited financial statements. These are portrayed as presenting a true and fair view. Interviews might investigate whether directors consider the actual extent the ‘true and fair view over-ride’ responsibilities placed on them when approving formal income statement and/or balance sheet presentations are usurped in practice by statutory conformity with accounting standards - because form prevails over substance. This study suggests that might be so for bearer-agricultural entities.

## 7.5 Concluding Comments and Recommendation

The research study revealed an institutional missing link – expected in regulatory organisation of business affairs but not in standard setting, on which the former relies.

Nearly two millennia ago, Juvenal in his Satires (Book VI, lines 347-8) posed the question: “*Quis custodiet ipsos custodes?*” – i.e. ‘Who will guard the guards themselves?’ Socrates in Plato’s Republic had previously posed a similar question of the guardians where the answer lay with the equivalent of Mitnick’s (1980) ‘Statesmen’ gatekeepers. But Mitnick also identified six other gatekeeper archetypes, some not so accommodating.

In modern times, most recently post-Enron, the question was further modified by e.g. Coffee (2006) – effectively, “*Who audits the auditors?*” The solution chosen in the U.S.A. for the auditor gatekeepers was Federal Sarbanes-Oxley legislation, coupled with overarching auditor regulation by the Public Company Accounting Oversight Board.

Evidence from this study suggests a further question: “*Who sets standards for the standard setters?*” For the *Agriculture* standard, the answer was an incomplete, introspective and unresponsive process. Error languished unattended and significant reports and recommendations went unpublished. There was no timely learning for improvements, including the AASB’s recommendation to separate IAS 41 in two.

None of the deficiencies surprised users. Processes lacked transparency and credibility. Lobbying concerns went unheeded; as did academic submissions from other perspectives. There were no checks and balances. The IASC Field Test did not show user support and the AASB’s PIR was in part an after-thought to facilitate IAS 41 transition to Australia.

Standard setting has become too important to commercial and financial businesses, for investors and for other users, to be left solely to gatekeepers’ internalised and remote purview acting without independent oversight and endorsement.

A final recommendation, directly resulting from the study, is that approval processes are enhanced to help international standard setting become more robust and credible. New

standards and revisions should be validated publicly by verification from independent commentators - drawn at least from academia, users and practitioners - appointed and operating independently, and on behalf of users; not dissimilar to the responsibilities of professional auditors appointed and responsible to act for and on behalf of shareholders.

The recommendation would therefore envisage that validation for new IASB standards and amendments, or recommendations from any post-enactment review process, occur quite separate from usual liaison with technical professionals and national standard-setter clients. An important objective should also be to verify internal consistency with other standards. The independent Validation Report would supply all submissions and reports, and contain staff and expert responses, including any minority reports and recommendations, as part of the promulgation process. The aim is to achieve a more transparent, consistent and credible process. Achievement of high-quality and universally-accepted standards risks being a chimera without that independent over-sight.

In September 2010, Sir David Tweedie conceded nine current standards are out of date, no longer meet the conceptual framework or are in need of overhaul. The *Agriculture* standard headed his list. This study confirms his assessment. It has taken over a decade to acknowledge a deficient standard was issued despite widespread adverse technical submissions and recommendations for improvements from practical experience.

Resolution will require another political process. The IASB Board will need to agree on agenda re-entrance to place IAS 41 back onto their formal agenda for review. To date, there appears to be little appetite to do so for this standard for at least another year. As a result, identified deficiencies continue.

The experience of the *Agriculture* standard is that such tardiness, lack of responsiveness, transparency and independent validation potentially devalues the suite of international accounting standards for users. It also erodes the professionalism and credibility of the IASB gatekeepers, and the adequacy of the IASB's institutional processes.

26th October, 2011

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**THE POLITICAL PROCESSES AND ROLE OF GATEKEEPERS  
IN SETTING ACCOUNTING STANDARDS  
FOR AGRICULTURE**

**APPENDICES 1-22**

**By**

**JOHN H.G. MILNE**

**A thesis  
submitted to The University of Sydney  
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requirements for the degree of  
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**Business School,  
The University of Sydney.**

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**Appendix 1: International Promulgations which Exclude Activities Associated  
with Agricultural Entities from their Scope**

**Australia**

AAS 2/AASB 1019 - Measurement and Presentation of Inventories

*'...does not apply to inventories that are...forests, livestock, or similar regenerative natural resources...'*

AAS 4/AASB 1021 – Depreciation of Non-Current Assets

*'...does not apply to non-current assets that are...forests, livestock, or similar regenerative natural resources...'*

AAS 10/AASB 1010 – Accounting for Revaluation of Non-Current Assets

*'does not apply to inventories...'*

FAS 2 - Valuation and Presentation of Inventories in the context of Historical Cost System specifically excludes *'forestry inventories'*.

**Denmark**

DAS 10 - Tangible Fixed Assets

*'...does not apply to forest and similar regenerative assets'*.

**IASC**

IAS 2 - Inventories

*'...other than - producers inventories of livestock, agricultural and forest products, and mineral ores to the extent they are measured at net realisable value in accordance with well established practices in certain industries'*.

IAS 4 - Depreciation Accounting

*'...except (for)... forests and similar regenerative natural resources'*.

IAS 16 - Property Plant and Equipment

*'...does not apply to forests and similar regenerative natural resources'*.

IAS 17 - Leases

*'...does not deal with... specialised types of leases:...lease agreements to explore for and or use natural resources'*.

IAS 18 - Revenue

*'...does not deal with revenue arising from... natural increases in herds, and agricultural and forest products'*.

**New Zealand**

FRS 4 - Accounting for Inventories

*'...does not apply to forest crops, farm produce and livestock held by the producer'*.

SSAP 3 - Accounting for Depreciation

*'...applies to all depreciable assets except ... forests and similar regenerative natural resources'*.

**South Africa**

AC 108 - Inventories

*'...excludes producers' inventories of livestock, agricultural and forest products'.*

AC 111 - Revenue

*'...excludes revenue arising from natural increases in herd, agricultural and forest products'.*

AC 123 - Property, Plant and Equipment

*'...does not apply to forests and similar regenerative natural resources'.*

**Sri Lanka**

SLAS 5 - Inventories 1c excludes...

*'...producers' inventories of livestock, agricultural products ... 'to the extent that they are measured at net realisable value in accordance with established practices in certain industries'.*

SLAS 8 – Accounting for Depreciation 4.a

*'...excludes... forests and similar regenerative natural resources'.*

SLAS 18 - Property, Plant and Equipment 3a

*'...excludes... forests and similar regenerative natural resources'.*

**Source:-** Appendix II Q.3 to Agenda Paper 9 – IASC Board Meeting; Brussels, March 1996.  
(Full text of Agenda Paper 9 in Appendix 7B below)

**Appendix 2: International Promulgations and Guidance for Preparation of  
Financial Information for Agricultural Production Entities**

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Institute of Chartered Accountants in Australia.

Accounting and Planning for Farm Management,  
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Department of Primary Industries, 1966, 1971.

**Canada**

Accounting and Financial Reporting by Agricultural Producers:  
A research study; Canadian Institute of Chartered Accountants, 1986.

Farm Accounting Standardization Manual,  
The Farm Accounting Standardization Review Committee;  
Government of Canada, 1991.

Model Financial Statements for Dairy Producers - Working Draft,  
Farm Accounting Standardization Task Force;  
Canadian Farm Business Management Council, 1995.

**Chile**

B#12 – Forestry Plantations.

**India**

Monograph on Accounting for Poultry Farming;  
The Institute of Chartered Accountants of India, 1980.

Monograph on Accounting for Rubber Plantations;  
The Institute of Chartered Accountants of India.

Monograph on Accounting for Agricultural Operations;  
The Institute of Chartered Accountants of India, 1983.

**Malaysia**

Accounting for Aquaculture;  
Malaysian Accounting Standard No.5, 1990.

Accounting for Pre-Cropping Costs;  
Draft Malaysian Accounting Standard, 1995.

Accounting for Plantation Companies;  
Exposure Draft, 1984.

**Netherlands**

GRAS publish chart of accounts and model financial statements for agriculture.

**New Zealand**

Farm Accounting in New Zealand;  
New Zealand Society of Accountants, 1965.

Current Value Techniques in Farm Accounting R-402;  
Toomath, C.R.; New Zealand Society of Accountants, 1973.

Management Accounting for the New Zealand Farmer R-404;  
New Zealand Society of Accountants, 1977, 1985.

Forestry Accounting: the report of a working party,  
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Department of Management Studies, University of Waikato, 1985.

Management Accounting for Horticulture R-406;  
New Zealand Society of Accountants, 1986.

Valuation of Livestock in the Financial Statements of Farming Enterprises;  
Technical Practice Aid No. 5. - New Zealand Society of Accountants, 1986.

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Research Bulletin No. 117 – Davy, A.R.; - New Zealand Society of Accountants, 1987.

Accounting for bloodstock enterprises;  
Technical Practice Aid No. 7. - New Zealand Society of Accountants, 1988.

Financial Reporting for Primary Producers;  
Clark, M.; - New Zealand Society of Accountants, 1989.

**Papua New Guinea**

Accounting for Plantations, Proposed Statement of Accounting Standard;  
Papua New Guinea Association of Accountants, 1990.

**South Africa**

Valuation of Livestock in the Financial Statements of Farming Enterprises,  
Accounting Guideline AC 205;  
The South African Institute of Chartered Accountants, 1988.

Accounting for Cooperatives,  
Accounting Guideline AC 206;  
The South African Institute of Chartered Accountants, 1989.

Guidelines for Annual Financial Statements of Primary Agricultural Cooperatives; Circular 9/91;  
The South African Institute of Chartered Accountants, 1991.

**Sri Lanka**

Accounting for Plantations, SLAS 32;  
The Institute of Chartered Accountants of Sri Lanka, 1993.

**Thailand**

Guideline for recording and disclosing activities of the dairy farming business.

**United Nations**

Accounting for Sustainable Forestry Management: A Case Study;  
United Nations Conference on Trade and Development, 1994.

**United States**

Statement of Position 85-3 – Accounting by Agricultural Producers and Agricultural Cooperatives;  
American Institute of Certified Public Accountants, 1985.

Audit and Accounting Guide – Audits of Agricultural Producers and Cooperatives with Conforming  
Changes as of May 1, 1994; (original issue, 1987)

Financial Guidelines for Agricultural Producers;  
Farm Financial Standards Task Force, 1991.

**Source:-** Appendix II, Q2 to Agenda Paper 9 – IASC Board Meeting; Brussels, March 1996.  
(Full text of Agenda Paper 9 in [Appendix 7B](#) below)



**Appendix 3: Listed Agricultural Companies in Australia and New Zealand**

**Australia**

(N.B. Some Companies were subsequently renamed, merged, taken over or de-listed.)

**Companies in Bold** are contained in the 1999 ASX Top-500; per Table 1  
Industry Representation analysis by Dowling and Godfrey (2001):

<b>Amalgamated Holdings Ltd</b>	<b>[AHD]</b>	Integrated Tree Cropping Ltd	[ITF]
<b>Amcor Ltd</b>	<b>[AMC]</b>	Lion Nathan Ltd	[LNN]
Atlas Pacific Ltd	[ATP]	Maryborough Sugar Factory Ltd	[MSF]
<b>Auspine Ltd</b>	<b>[ANE]</b>	<b>McGuigan Simeon Wines Ltd</b>	<b>[MGW]</b>
Australian Agricultural Company Ltd	[AAC]	Nanon Cotton Co-op	[NAM]
<b>Australian Food and Fibre Ltd</b>	<b>[AFF]</b>	<b>Newhaven Park Stud Ltd</b>	<b>[NPS]</b>
Australian Plantation Timber Ltd		<b>Normans Wines Ltd</b>	<b>[NMW]</b>
Australian Vintage Ltd	[AVL]	<b>North Broken Hill Peko Ltd</b>	
Australian Wine Ltd	[AWL]	Palandri Wine Investments Ltd	
<b>Brian McGuigan Wines Ltd</b>	<b>[MGW]</b>	PaperlinX Ltd	[PPX]
<b>BRL Hardy Ltd</b>	<b>[BRL]</b>	<b>Petaluma Ltd</b>	<b>[PLM]</b>
<b>Cabonne Ltd</b>	<b>[CBW]</b>	<b>Peter Lehman Wines Ltd</b>	<b>[PLW]</b>
<b>Carter Holt Harvey Ltd</b>	<b>[CAH]</b>	<b>Pipers Brook Vineyard Ltd</b>	<b>[PBV]</b>
Challenger Wine Trust	[CWT]	Queensland Cotton Ltd	[QCH]
Cheviot Killybilly Vineyard Prop Group	[CKP]	Reynolds Wines Ltd	[RYW]
Chiquita Brands South Pacific Ltd	[CHQ]	<b>Ridley Corporation Ltd</b>	<b>[RIC]</b>
Cockatoo Ridge Wines Ltd	[CKR]	<b>Select Harvests Ltd</b>	<b>[SHV]</b>
<b>Cranswick Premium Wines</b>	<b>[CEW]</b>	Simon Gilbert Wines Ltd	[SGV]
<b>CSR Ltd</b>	<b>[CSR]</b>	<b>Southcorp Ltd</b>	<b>[SRP]</b>
Deep Sea Fisheries Ltd	[DSF]	<b>Sydney Aquarium Ltd</b>	<b>[SAQ]</b>
Dromana Estate	[DMY]	<b>Tandou Ltd</b>	<b>[TAN]</b>
East African Coffee Plantations Ltd	[EAC]	<b>Tassal Group Ltd</b>	<b>[TSS]</b>
Evans & Tate Ltd	[ETW]	<b>Timbercorp Ltd</b>	<b>[TIM]</b>
<b>Fletcher Challenge Group Ltd</b>	<b>[FCL]</b>	Vealls Ltd	[VEL]
Forest Enterprises Australia Ltd	[FEA]	<b>Wesfarmers Ltd</b>	<b>[WES]</b>
<b>Fosters Group Ltd</b>	<b>[FBG]</b>	<b>WESFI Ltd</b>	
<b>Futuris Corporation Ltd/Elders Ltd</b>	<b>[MGA]</b>	Willmott Forests Ltd	[WFL]
Global Seafood Ltd	[GSF]	Xanadu Wines Ltd	[XAN]
Great Southern Plantations Ltd	[GSP]	Yates Ltd	[YTL]
<b>Gunns Ltd</b>	<b>[GNS]</b>		

**New Zealand**

(N.B. Some Companies were subsequently renamed, merged, taken over or de-listed.)

Carter Holt Harvey Ltd	[CAH]	Rubicon Ltd	[RBC]
Delegats Wine	[DGL]	Rural Equities Ltd	[REQ/REL]
Evergreen Forests	[EVF]	Sanford Fisheries Ltd	[SAN]
Fletcher Forests Ltd/Tenon Ltd	[TEN]	Satara Co-operative Group Ltd	[SAT]
Livestock Improvement Group Ltd	[LIC]	Seeka Kiwifruit Industries Ltd	[SEK]
The New Zealand Wine Company Ltd	[NWC]	Silver Fern Farms Ltd	[SFF]
Nuhaka Forests	[NUH]	Tasman Farms Ltd	[TFL]
NZ Farming Systems Uruguay Ltd	[NZS]	Te Kairanga Wines Ltd	[TEKAINGA]
NZ Forestry Plantations Ltd		Terra Vitae Vineyards Ltd	[TERRAVITAE]
NZ Superannuation Fund		Turners & Growers Ltd	[TUR]
Opio Forestry	[OPI]	Whakatu Afforestation Trust	[WHA]
Oyster Bay Marlborough Vineyards Ltd	[OBV]	Zespri Group Ltd	[ZGL]

**Some significant 'Overseas' Companies in Australia & NZ responding to IAS 41 – or US-GAAP**

- Allied Domecq [France] – Montana NZ Vineyard interests
- Cape Mentelle [France] – Moet Hennessy West Australian Vineyard interests
- Constellation Wines [US] – BRL Hardy Vineyard interests
- Cloudy Bay [France] – Cape Mentelle's Marlborough NZ Vineyard interests
- Hancock Natural Resources Group [US] – NZ Forestry interests
- Harvard Management Company [US] – Kaingaroa Timberlands [Forest] interests
- Oji Paper [Japan] – Pan Pac Forest Products NZ Forestry interests
- Rayonier Ltd [US] – NZ Forestry interests
- Wenita Forest Products Ltd [China/US] – NZ Forestry partnership interests

**Source:** ASX and NZX Listings

## **Appendix 4: Pre-SGARA Forestry Accounting Policies and Practice in Australia**

The Tables on the following four pages are extracted direct from the Herbohn K.F., R. Peterson and J.L. Herbohn article: 'Accounting for Forestry Assets: Current Practice and Future Directions' *Australian Accounting Review*, Vol. 8 (No.1); pp. 59-63, 1998.

They illustrate the wide diversity of accounting practice in their comprehensive analysis of a significant group of Australian forestry entities in the public and private sectors. No two entities had common accounting policies for measurement, income recognition and balance sheet categorisation. The sample includes two New Zealand major forestry companies then listed on the ASX: Carter Holt Harvey Limited and Fletcher Challenge Limited.

Table 2 lists the 13 respondent entities - excluding the Northern Territory Department of Primary Industries and Fisheries because it did not disclose significant forestry interests. The Table includes footnotes relevant to State Forestry entities in particular.

Table 3 records the different valuation methods reported in respective entity financial statements. The footnotes elaborate on respective reported valuation methodologies.

Table 4 summarises whether or not changes in carrying values were recorded; and, if so, whether in reserves or in the income statement, with additional footnote commentary about each entity's policy and accounting treatment.

Finally, Table 5 records how forestry assets were classified in respective entity balance sheets.

ED 83 retains the DP 23 recommendations on balance-sheet disclosure. In particular, SGARAs are to be presented separately in the balance sheet, without classification into current and non-current portions (para. 5.1, ED 83). The exposure draft also prescribes certain non-financial disclosures which are generally consistent with the DP 23 recommendations. In particular, the following information must be disclosed:

- the nature and quantity of SGARAs; and
- the total and restricted amounts of SGARAs, together with details of the nature and extent of those restrictions (para. 6.1).

However, two modifications were made to the DP 23 recommendations and incorporated into ED 83. First, all reference to environmental information has been removed from ED 83. Second, if a surrogate measure for net market value has been used, ED 83 requires that the following should be disclosed:

- the method;
- any significant assumptions;
- information to assess value sensitivity to changes in underlying assumptions; and
- whether the valuation is an independent or directors' valuation (para. 6.1).

**REVIEW OF CURRENT**

**AUSTRALIAN FORESTRY ACCOUNTING PRACTICE**

The forestry reporting practices of a sample of Australian reporting entities were surveyed to enable the recommendations of DP 23 and ED 83 to be evaluated in the context of current reporting practice. The sample comprised all ASX-listed companies involved in forestry (identified by classification under the standard industrial category of Agriculture, Forestry and Fishing), additional private-sector entities identified in the discussion paper<sup>11</sup> and all state forestry authorities. These entities were requested to provide financial statements for the period 1991 to 1995. All of the eight private-sector organisations responded to this request, and six out of seven state forestry authorities were willing to co-operate.<sup>12</sup> The Department of Primary Industry and Fisheries (Northern Territory) did not disclose any significant forest investments and was excluded from the survey. Details of the survey sample are set out in Table 2.

The financial statements were surveyed to determine forestry accounting practices in relation to:

- valuation of forestry assets;
- recognition and measurement of value changes;
- balance-sheet classification of forestry assets; and

**TABLE 2: SAMPLE OF AUSTRALIAN REPORTING ENTITIES SURVEYED (1990-95)**

<i>Private-sector corporations</i>	<i>Public-sector organisations (state forestry authorities)</i>
<b>N=8</b>	<b>N=5</b>
Ancor	Department of Conservation and Land Management (Western Australia) <sup>B</sup>
AUSPINE <sup>A</sup>	Department of Conservation and Natural Resources (Victoria) <sup>C</sup>
Carter, Holt and Harvey	Forestry Commission of Tasmania
CSR	Queensland Department of Primary Industries (QDPI)
Fletcher Challenge	Forest Services <sup>D</sup>
North Ltd <sup>A</sup>	State Forests of NSW
Wesfarmers <sup>A</sup>	
Westralian Forest Industries (WESFI)	

- A Given the time frame of the study (1990-95), there were several mergers/acquisitions and sell-outs. AUSPINE acquired SEAS-SAP-FOR (1994), Wesfarmers acquired Bunnings Ltd (1994) and North Broken Hill Peko Ltd rationalised its operations to become North Ltd.
- B Although the Department of Conservation and Land Management (Western Australia) suggested that accrual accounting reports would be available for the 1994/95 period, the department's financial statements were prepared on a cash basis. Activities were divided into programs and statements of cash receipts and cash payments were prepared for each program. These were unsuitable for review in terms of the valuation of forest assets and the recognition of value changes in these assets and balance-sheet disclosure.
- C The Victorian Department of Conservation and Natural Resources has been granted an exemption by the Ministry of Finance from preparing a full set of audited financial statements for the 1994/95 financial period and so prepared its statements on a cash basis. An unaudited supplementary set of accrual-based financial statements were provided and these supplementary statements were used only to assess disclosure of non-financial, environmental information.
- D The Queensland Department of Primary Industries Forest Services prepared its statements on a cash basis, but also produced a Statement of Assets and Liabilities. Consequently, it was only excluded from analysis of the valuation of forest assets and the recognition of value changes in these assets.

**TABLE 3: VALUATION METHODS FOR FOREST ASSETS IDENTIFIED IN FINANCIAL STATEMENTS (1990-95)**

Entity	Historical cost in primary statements		Alternative valuation in primary statements		
	Hist. cost only	Lower of hist. cost or market value	Recoverable amount	Net present value	Other
<b>Private sector:</b>					
Ancor		(A&D&F)			
AUSPINE		(A&D&E&F)			
Carter, Holt & Harvey				(C)	
CSR				(B&C&E&G)	
Fletcher Challenge		(D&F)			
North Ltd				(B&C)	
Wesfarmers	(D&E&F)				
Westralian Forest Indust. (WESFI)				(B&C)	
<b>Public sector</b>					
Dep't Cons. & Land Manag't (WA)**					
Dep't Cons. & Nat. Res. (Vic)**					
Forestry Comm. (Tas.)			(G&H)		
QDPI Forest Services**					
State Forests of NSW	(I)		(I)		(I)

\*\* Department of Conservation & Land Management (WA), Department of Conservation & Natural Resources (Vic.) and Queensland Department of Primary Industries did not report values for forest assets and so their sets of statements were unsuitable for analysis.

**Legend:**

- A Entities adopting this approach valued forests at the lower of historic cost or recoverable amount. Recoverable amounts were generally estimated as the volume of merchantable timber multiplied by current or average royalty prices. This would normally result in the use of historic cost since it would normally be less than recoverable amount unless there had been a natural disaster (eg, flood, fire, pestilence).
- B Forest assets are initially recorded at cost and then growing timber at recoverable amount. It is different to Method A in that recoverable amount is estimated using present value calculation, and the lower of cost or market value rule is not used.
- C Net present value. Calculated using (1) estimates of timber volume from forest, and (2) estimates of the associated future cash inflows (eg, sales) and outflows (eg, harvesting and distribution costs). These net cashflows were discounted using a selected discount rate. Carter, Holt & Harvey used an 8% discount rate and has not revalued its forest assets since 1993. CSR, North Ltd and WESFI did not disclose the discount rates used.
- D Any associated interest costs were capitalised as part of the cost of the forest asset.
- E Timber access rights/log licenses were disclosed separately from standing timber at cost (the exception was CSR which disclosed these rights at recoverable amount) less accumulated amortisation. While Wesfarmers disclosed timber rights, no amortisation was recorded.
- F The stand/unit method was used to determine historic cost. State Forests of NSW only used this method for non-commercial plantations. Wesfarmers gave no clear indication of the policy adopted, but on balance the general statement of accounting practice would suggest that the stand/unit method was adopted.
- G Maintenance costs for mature stands were treated as expenses when incurred.
- H The Forestry Commission (Tas.) used current replacement cost for growing, non-merchantable trees, which comprised trees < 12 to 15 years old. Mature trees at clearfell age were usually > 12 to 15 years old and were valued at recoverable amount.
- I State Forests (NSW) valued commercial pine forests using the methods outlined in A above, but did not apply the lower of cost or market rule. Its non-commercial broadleaf forest assets were valued at cost (last capitalised 1983/84) adjusted by the CPI (last adjusted 1991) and its Cyprus pine and native broadleaf forests assets were valued at unadjusted historic cost. The sustained yield method was used for its broadleaf, cypress pine and native plantations (expenditure last capitalised 1984).

TABLE 4: METHODS OF RECOGNITION OF VALUE CHANGES IN FORESTRY ASSETS IDENTIFIED IN FINANCIAL STATEMENTS (1990-95)			
Entity	No recognition until timber harvested	Recognition as a capital adjustment	Recognition as an income adjustment
<b>Private sector:</b>			
Ancor	(C)		
AUSPINE	(C)		
Carter, Holt & Harvey		(A&B&D)	
CSR			(E)
Fletcher Challenge	(C)		
North Ltd		(A&B&D)	
Wesfarmers	(C)		
Westralian For. Indust. (WESFI)		(A&B&D)	
<b>Public sector:</b>			
Dep't Cons. & Land Manag't (WA)**			
Dep't Cons. & Nat. Res. (Vic.)**			
Forestry Comm. (Tas.)		(A&B&D)	
QDPI Forest Services**			
State Forests (NSW)	(F)	(F)	(F)

\*\* Department of Conservation & Land Management (WA), Department of Conservation & Natural Resources (Vic.) and Queensland Department of Primary Industries did not report values for forest assets and so their sets of statements were unsuitable for analysis.

**Legend:**

- A The balance of any excess of value decrement over the amount in the reserve was closed to the profit and loss statement. Although this policy was adopted by WESFI, it was not implemented during the survey period because the last revaluation occurred in 1993.
- B Recognition of value changes was made on the basis of periodic assessment of, *inter alia*, changing timber volumes and increasing royalty rates. Reference was made to revaluations occurring on a periodic basis in the financial statements of Carter, Holt & Harvey (last revaluation 1993), North (annual basis) and WESFI (last revaluation 1993). The Forestry Commission (Tas.) used growth models to provide annual estimates which were generally checked against physical data at five-yearly intervals. The capital-maintenance adjustments were made against the following reserves:
  - Asset Revaluation Reserve - Carter, Holt & Harvey;
  - Regenerative Resource Reserve - North Ltd;
  - Forest Timber Revaluation Reserve - Forestry Comm. (Tas.); and
  - Asset Revaluation Reserve - WESFI.
- C The accumulated historical cost of the forest assets (net of thinning revenue) was matched with associated revenues from harvesting the timber. This policy was not explicitly outlined in Wesfarmers' financial statements, but it would be consistent with their general forestry accounting practice.
- D The carrying amount of the forest assets (after periodic revaluations) is charged against associated revenue from harvesting the timber. The exception to this is North which reverse the revaluation adjustment so that the result from the sale is recorded by reference to historic cost.
- E CSR recognised value changes on the basis of periodic assessment of, *inter alia*, changing timber volumes valued at commercial rates, presumably on an annual basis (no explicit indication of the time-scale involved was given). The changes were made as adjustments to income (ie, operating profit before tax and abnormal items) and the non-current asset, growing timber. All period expenses relating to growing timber are charged against income in the profit and loss account.
- F State Forests of NSW disclosed a detailed analysis of changes in the value of growing trees in the notes (1995, Note 10, p. 88). In particular, a market value increment (MVI) was calculated for its pine plantations which summarised the value of changes due to timber price and volume. The MVI was closed to the profit and loss account and then treated as a transfer to the growing stock revaluation reserve. Value changes for broadleaf and Cyprus pine forests and native plantations have been ignored since 1991 and so were not recognised until the timber was actually harvested.

least two reasons.

First, despite the enthusiasm of the authors of DP 23 for adoption of a productive capacity concept of capital, on which their recommendations are based,

the concept has not been officially endorsed in any accounting standard or statement of accounting concepts – other than in SAP 1 *Current Cost Accounting*, which is largely ignored by practitioners, including

**TABLE 5: BALANCE-SHEET CLASSIFICATION OF FORESTRY ASSETS IDENTIFIED IN FINANCIAL STATEMENTS (1990-95)**

Entity	Asset class independent of current and non-current classification	Classification as non-current asset		
		Separate class	Property, plant & equipment	Other non-current assets
<b>Private Sector:</b>				
Ancor			(A)	
AUSPINE				(B&D)
Carter, Holt & Harvey		(C)		
CSR			(A&D)	
Fletcher Challenge			(A)	
North Ltd	(E)			
Wesfarmers			(A&D)	
Westralian For. Ind. (WESFI)				(B&D)
<b>Public Sector:</b>				
Dep't Cons. & Land Manag't (WA) **			(A)	
Dep't Cons. & Nat. Res. (Vic.) **				
Forestry Comm. (Tas.)		(C&F)		
QDPI Forest Services		(C)		
State Forests (NSW)		(C&F)		

\*\* Department of Conservation & Land Management (WA) and Department of Conservation & Natural Resources (Vic.) did not report values for forest assets and so their sets of statements were unsuitable for analysis.

**Legend:**

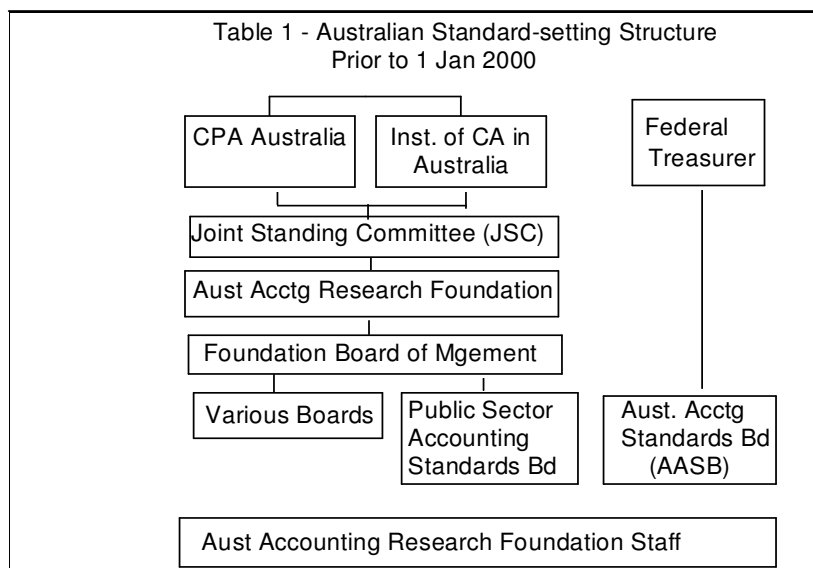
- A Sub-categories used within the category of property, plant and equipment were:
  - Standing timber - Ancor;
  - Growing timber - CSR;
  - Forest and resource extraction assets - Fletcher Challenge; and
  - Standing timber - Wesfarmers.
- B The sub-categories used within the category of other non-current assets were:
  - Standing timber - AUSPINE; and
  - Investments - WESFI.
- C The sub-categories used within the separate class of non-current assets were:
  - Forest assets - Carter, Holt & Harvey;
  - Inventories (forest assets) - Forestry Comm. (TAS.)
  - Forest regenerative assets - QDPI; and
  - Growing stock - State Forests (NSW).
- D Separate disclosure of timber access rights/log licences less accumulated amortisation (Wesfarmers did not disclose accumulated amortisation).
- E North Ltd disclosed its forest holdings as a separate class of asset to the traditional classification of current and non-current assets. This new asset class was titled Regenerative Resource. However, there was no disclosure of the allocation of the value of this asset between current and non-current asset classes.
- F Forestry Comm (Tas.) and State Forests of NSW. were the only entities to draw a distinction between current forestry assets (ie, stores and seedlings) and non-current forestry assets (ie, standing timber) in the primary statements. The current forest asset classes were titled Inventories and Growing stock respectively.

## Appendix 5: Australia's Institutional Framework Pre- and Post- 1 January 2000.

The description and tables below are summarised from information provided by Mr Bruce Porter, Partner - Deloitte Touche Tohmatsu, on the historic overview of the standard setting environment surrounding the development of the AASB 1037 SGARA Agriculture standard in Australia.

The summary is derived from a much longer description extracted from his joint publication *Australian GAAP* (Parker and Porter, 2002).

Up to and including the release of the AASB 1037/AAS 35 SGARA accounting standards in May 1998, the standard setting institutional framework was as follows:



**Source:** Australian GAAP, 2002, by Colin Parker and Bruce Porter, p. 28.

The AARF was the principal working group for accounting research and standard setting. It supported both the Australian Accounting Standards Board (AASB) and the Public Sector Accounting Standards Board (PSASB).

Each Board issued its own Standards. The two series of accounting standards were:

- Australian Accounting Standards Board standards - the AASB series. They applied to companies, disclosing entities and registered schemes that were reporting entities regulated by the Corporations Law. These Standards were mandatory in the preparation of financial statements by reporting entities; and
- Statements of Australian Accounting Standards - the AAS series. They applied to reporting entities not required to apply the AASB Accounting Standards. These entities were generally non-corporate reporting entities in the private and public sectors. The standards were professionally backed by dint of professional sanction against members for non-compliance.

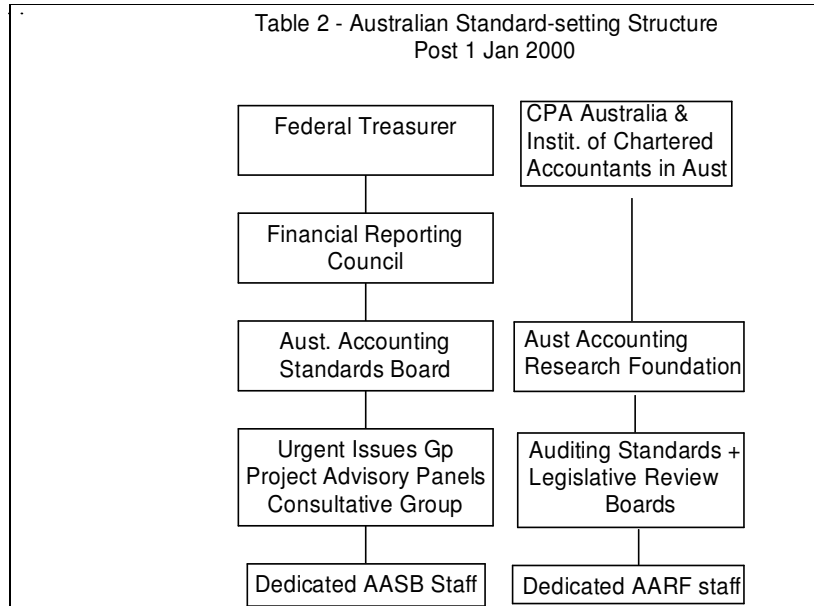


### Corporate Law Economic Reform Program – effective post 1 January 2000

As part of the Policy framework for the Corporate Law Economic Reform Program (CLERP-1), announced in March 1997, the Federal Government proposed to update the general Corporations Law and related Federal corporate/securities regulation.

This was designed to reflect modern international trends including setting accounting standards; harmonisation of standards with the IASC and New Zealand; directors' duties; corporate governance; and other related matters.

The revised and simplified post-CLERP standard setting structure was as follows:-



**Source:** Australian GAAP, 2002, by Colin Parker and Bruce Porter, p.29.

As originally proposed the Australian Accounting Standards Committee (AASC) was to replace the AASB and the PSASB as the body which prepared, approved and issued a common set of accounting standards for the public and private sectors.

Subsequently, the AASC was renamed the Australian Accounting Standards Board, as shown in Table 2 above. From 1 June 2000 all subsequent standards were issued in the single AASB series.

## **Appendix 6: AARF Project Brief**

### **“Accounting for Self-Generating and Regenerating Assets”**

#### **1. Objective**

In the context of the Conceptual Framework for general purpose financial reporting, the objective of this project is to set accounting standards for the measurement and disclosure of self-generating and regenerating assets, and for other issues in relation to those assets, such as the timing of revenue recognition for the operations they are employed in.

#### **2. Approach**

Each task in the development of these accounting standards, including the preparation of the discussion paper, is to be undertaken by reference to the building blocks of a Conceptual Framework (as identified by the Foundation) and to material prepared to date in respect of that Framework. This approach is designed to ensure a comprehensive and consistent approach to each issue. As an example, the arguments raised should be considered in the light of the proposed Statements of Accounting Concepts “Objective of General purpose Financial Reporting” and “Qualitative Characteristics of Financial Information”.

#### **3. Scope delimiters**

The following issues are excluded from the scope of this project:

Issue i) is addressed in other projects of the Foundation.

Issue ii) is largely unrelated to the self-generating or regenerating nature of the types of assets which have been indicated as falling within the scope of the project.

However, such topics may be referred to in drawing together the various issues, or in identifying common deficiencies in reporting for self-generating and regenerating assets.

As this project is concerned with general purpose financial reporting, its scope does not include the information needs of special purpose users such as managements. For example, the usefulness or otherwise of “direct costing” of regenerating assets for management decision-making is beyond the scope of this project.

## Points for Consideration in Preparation of a Discussion Paper

### “Accounting for Self-Generating and Regenerating Assets”

#### 1. Literature Review

A detailed review of academic and professional literature on the topic of self-generating and regenerating assets, other than those matters excluded in the Scope Delimiters Section of the project brief. Overseas as well as Australian literature is to be reviewed and the professional pronouncements (and post-implementation reviews) of all major overseas bodies are to be considered (IASC, US, Canada, UK, NZ, South Africa).

#### 2. Overview of the activities and “industry”

Identification of the types of activities encompassed by this project: such activities may include agriculture, aquaculture, animal husbandry, biotechnology development, dairying and lot feeding, forestry, horticulture/viticulture, and salt farming (*sic*).

A broad overview of the types of entities, and scale of their operations – sales, assets, etc. – which use self-generating and regenerating assets in their operations.

#### 3. Survey of Financial Reports

Review the financial reports of a suitable number of reporting entities of various sizes and types from both the public and private sectors. From review of reports, compile and analyse data re:

- accounting policies employed in relation to: basis of asset valuation; timing of revenue recognition in respect of the earning process; consistency of those policies with those applied by the entity to other assets, revenues and expenses.
- disclosures in respect of those assets and their consumption – *e.g.* classification in the statement of financial position; disclosure of consumption of such assets in the operating statement.

#### 4. Identification of Issues

- A. Defining “Self-generating and regenerating assets” for the purpose of an Australian Accounting Standard, and in the process, identifying the unique or particular characteristics of the category of assets;
- B. Appropriate **measurement basis** of accounting for:
  - self-generating and regenerating assets, having regard to the meaning of “service potential” thereby ascribed
    - i) to those assets and its relevance to economic decision-making by users of general purpose financial reports; and
    - ii) assets used in conjunction with self-generating assets, such as land, quota licences, plant and equipment.

Implications of the classification of livestock between “breeding” or “productive” livestock and “trading” livestock for the appropriate measurement basis for self-generating and regenerating assets.

If a market value model is argued, should the following components of changes in total market values be treated differently?

- i) change due to physical growth;
- ii) change due to unit value movements.

Where cost-based valuation methods are discussed, consideration of which costs ought to be identified as relevant to self-generating and regenerating assets; for example, interest on borrowings used to finance growing assets prior to completion of their growth process.

**C.** Identification of the appropriate **timing of revenue recognition** with respect to the growth/natural reproduction, and subsequent sale of self-generating and regenerating assets; having regard to implications for the reporting of the entity’s performance in achieving its objectives during the reporting period – including identification of the implications of arguments thereby developed for the existing requirements of Australian Accounting Standard AAS 10 / Approved Accounting Standard ASRB 1010 “Accounting for the Revaluation of Non-Current Assets”.

**D. Disclosure issues** which arise in the application of the tentative building blocks of a Conceptual Framework to the characteristics of self-generating and regenerating assets and of their usage in the operations of reporting entities. For the purpose of illustration, disclosure issues that could be raised for the Boards’ consideration may include such matters as:

- i) Criteria for dissection of self-generating/regenerating assets in the statement of financial position; *e.g.* current/non-current classifications, and dissection of trading/breeding livestock;
- ii) Appropriate disclosures in respect of multiple usage of assets which are the subject of this project; *e.g.* State forests which generate revenues from logging and from recreational usage; and
- iii) Relevance of disclosure of firm (unperformed) sales contracts.

**E. Other issues:**

Relevance on non-financial information to assessments of the entity’s performance; and

Brief consideration of the appropriate frequency of reporting by entities with self-generating and regenerating assets, *i.e.* having regard to the operating cycle.

## **5. Analysis of Issues Identified**

Where possible, practical examples of alternative methods, disclosures, etc., should be given to assist readers in understanding the different methods, disclosures, etc., and to assist in analysing the impact of the choice of one alternative over another.

Arguments proposed in respect of issues identified in Item 4 above should be analysed in terms of the tentative building blocks of a Conceptual Framework, as identified by the Foundation. Where the Foundation has prepared material regarding any of the building blocks, for instance Accounting Theory Monographs or proposed Statements of Accounting Concepts, that material is to be used as a primary reference. Any inconsistencies identified in the tentative building blocks during the course of the study should be noted.

## **6 Conclusions and Recommendations**

The discussion paper should conclude by drawing together the information presented in previous chapters and making recommendations regarding proposed accounting standards relating to accounting for self-generating and regenerating assets – including transitional provisions if considered appropriate – with supporting reasons.

AARF Cover Letter addressed to:

Mr D.L. Roberts,  
Project Leader – Self Generating Assets Research,  
Department of Accounting and Financial Management,  
The University of New England,  
ARMIDALE NSW 2351

Signed by Warren J. McGregor, Director.  
13 July 1990

Entitled “Self-Generating and Regenerating Assets”  
With Attachments

- Agreement with Project Contractor
- Project Brief.

**Source:**- Dr. J.J. Staunton Private Papers

**Appendix 7A: IASC Project Proposal – Agriculture**  
**(including growing crops, plantations and forests, and livestock)**

1. The purpose of the proposed project is to develop an International Accounting Standard on the recognition, measurement and disclosure in financial statements of assets, liabilities, income and expenses resulting from activities in agriculture.

**The Need for an International Standard**

2. The main objective of IASC is to develop International Accounting Standards that are relevant in the published financial statements of all businesses in all countries. IASC also develops Standards that deal with accounting issues that arise in particular industries when those issues might require different standards or implementation guidance and when the industry is significant and influential internationally.
3. Agriculture is a significant industry in many countries. For example, agriculture accounts for between 25% and 50% of the gross national product of many developing countries and employs approximately 20% of the population in countries in East and Central Europe. Many governments provide substantial grants, subsidies and other assistance to agricultural enterprises. Agriculture is also a major consumer of capital; for example, it accounts for approximately 20% of the World Bank's total volume of lending and almost 30% of the cumulative lending of the African Development Bank.
4. In these circumstances, there is widespread interest in the financial performance, financial position and cash flows of enterprises operating in Agriculture. In particular, investors, lenders and governments need relevant, reliable and comparable financial information from different enterprises involved in agriculture. Compliance with accounting standards that require use of like treatments for like transactions and events will help achieve that objective.
5. Enterprises involved in agriculture can and do apply the same accounting standards that apply to other enterprises. However, the nature and operations of agriculture are such that they give rise to a number of accounting issues which are different from those that arise in other industries. These issues include:
  - the recognition and measurement of revenue arising from self-generating or regenerating assets such as livestock, growing crops and plantations;
  - the measurement of inventories and cost of sales on the sale of such items as the progeny of breeding livestock and annual crops from long-lived plantations;
  - the recognition and amortisation of development expenditure on long-lived assets such as forests and plantations;
  - the measurement of performance on long-lived assets such as forests and plantations that require inputs of resources over a lengthy period before revenue is generated;
  - the recognition and measurement of government quotas, governmental subsidies and other government assistance; and
  - the appropriate accounting treatment and disclosure for shared facilities, co-operatives and similar arrangements.

6. Some national standard setting bodies have issued, or are developing, special requirements or guidelines on these or similar accounting issuers. For example:
  - France has issued a general accounting plan for agricultural business;
  - Malaysia, New Zealand, Papua New Guinea and Sri Lanka have issued guidance on accounting issues arising from plantations and forests;
  - New Zealand and South Africa have issued guidance on accounting for livestock;
  - Malaysia has issued an accounting standard on aquaculture;
  - Australia is preparing a research study on self-generating and regenerating assets (including agriculture, aquaculture, livestock, horticulture, viticulture and forestry); and
  - Malawi has added guidance to IAS 2, Inventories to cover growing crops and harvested crops awaiting sale.
  
7. There is similar, if not greater, need for an International Accounting Standard on accounting issues arising from agriculture. Agriculture is a worldwide industry and IASC has not yet dealt with these accounting issues. It has therefore excluded certain agricultural activities from its General Standards – for example, those on inventories, property, plant and equipment, and revenue. Countries that make extensive use of International Accounting Standards, such as Nigeria and Zimbabwe, have urged IASC to deal specifically with agricultural issues. A survey by the Farm Development Division of Agriculture, Canada, suggested that standardisation of financial reporting in agriculture would “improve the industry no end”.
  
8. An International Accounting Standard on agriculture issues would improve the relevance, reliability and comparability of published financial statements of enterprises involved in agriculture. The International Accounting Standard would assist developing countries and be influential in developed countries. The Standard could be used:
  - as a national accounting requirement by countries that use International Accounting Standards as their national requirements. Many of these countries are developing countries in which agriculture makes a significant contribution to gross national product;
  - as the basis for a national requirement by countries that use other International Accounting Standards in such a way. Agriculture also plays a significant part in the economies of many such countries;
  - as the basis for a national requirement in those developed countries that usually develop their own national requirements but which support IASC and would be willing to use the International Accounting Standard in any case; and
  - as part of the reporting requirements imposed by development banks. Many such banks already require borrowers to report in conformity with International Accounting Standards. These reporting requirements are incomplete if they do not include a Standard that deals with assets, liabilities, income and expenses, as well as disclosures, resulting from agricultural activities.

### **Scope of the Proposed International Accounting Standard**

9. The proposed International Accounting Standard will deal with the recognition, measurement and disclosure of assets, liabilities, income and expenses resulting from the following agricultural activities:
  - Growing crops;
  - Forestry and plantations; and
  - Livestock.
  
10. The proposed Standard will supplement existing International Accounting Standards which should also apply to assets, liabilities, income and expenses arising from agriculture unless they are specifically exempted by a particular Standard. Therefore, the project will consider the relevance of existing International Accounting Standards, such as those dealing with inventories, property, revenue and government grants and assistance. It will specifically address existing exemptions for agricultural assets, income and expenses in those Standards. It will also consider the relevance of items on IASC's future work programme, including a possible Standard on environmental assets and liabilities.
  
11. The project will consider the need for additional International Accounting Standards or additional implementation guidance. It will also consider any accounting implications of particular forms of business entities, such as co-operatives and shared processing facilities, that are used by some agricultural enterprises.

### **Due Process**

12. The project will follow IASC's normal due process, including the development and publication of a Draft Statement of Principles and an Exposure Draft of the proposed International Accounting Standard. The IASC Board will be requested to:
  - add the project to its work programme (1994);
  - review and comment on progress reports and the research (1994/95); and
  - approve the Statement of Principles, Exposure Draft and International Accounting Standard.
  
13. The project will be under the supervision of a Steering Committee which will include representatives of professional accounting bodies and other interested organisations. The members of the Steering Committee will be chosen for their experience and knowledge of the issues involved, their expertise in addressing accounting standards generally, and their concern for relevant, reliable and internationally comparable financial information.



## Work Programme and Timetable

### Research Study

14. As the first stage in the project, the IASC staff will prepare a research study that will consider:
  - the nature of the possible accounting issues that should be dealt with in the project;
  - any special needs of the users of financial statements of agricultural enterprises;
  - the current requirements and practices that are applied around the world to these accounting issues and the reasons for those requirements and practices;
  - possible solutions to those accounting issues; and
  - the scope for improvement and harmonisation of financial statements of agricultural enterprises.
15. The research study will consider these issues from international and regional perspectives.
16. This stage of the project will involve consultations with, amongst others:
  - National standard setting bodies and other organisations that have considered or are considering the accounting issues relating to agricultural enterprises;
  - Academics who are studying these issues;
  - Financial institutions, including development banks, that are providing finance and other assistance to agricultural enterprises;
  - Other users of the financial statements of agricultural enterprises;
  - Financial executives of agricultural enterprises;
  - Accounting firms; and
  - National and regional accounting bodies.
17. This first stage of the project will take approximately one year and will involve two meetings of the Steering Committee. The first meeting will take place fairly early in the process and will help determine the work programme, the scope of the project and nature of the research and consultations. The second meeting will take place after most of the consultations and research have taken place.

### Draft Statement of Principles

18. The second stage of the project will involve the development and publication by the Steering Committee of a Draft Statement of Principles. The purpose of a Draft Statement of Principles is to:
  - set out arguments for and against the development of an International Accounting Standard on the topic;
  - set out the accounting principles that will form the basis of an Exposure Draft of the proposed International Accounting Standards. The principles will be supported, where appropriate, by proposed implementation guidance; and
  - describe the alternative solutions considered and the reasons for recommending their acceptance or rejection.
19. In view of the wide range of issues and the complexities involved, the development of the Draft Statement of Principles will take approximately six to nine months and require two meetings of the Steering Committee.
20. After it has been approved by the Steering Committee, the Draft Statement of Principles is issued for public comment. During the comment period, the Project Manager will actively seek comments from interested organisations and individuals.

Statement of Principles

21. In the next stage of the project, the Steering Committee will reconsider the Draft Statement of Principles in the light of the comments received and approve a final Statement of Principles for approval by the Board. On the assumption that the comments generally support the Draft Statement of Principles, this stage of the project will take four to six months from the comment deadline. It will require one meeting of the Steering Committee.

Exposure Draft of Proposed International Accounting Standard

22. Once the Board has approved the Statement of Principles, the Steering Committee will prepare an Exposure Draft of the proposed Accounting Standard for approval by the Board. The Exposure Draft is based on the principles and guidance in the Statement of Principles. On the assumption that no unforeseen difficulties or new ideas arise, this stage of the project will take four months from the Board's approval of the Statement of Principles to the Board's approval of the Exposure Draft. It will require one meeting of the Steering Committee. After it has been approved by the Board, the Exposure Draft is issued for public comment. During the comment period, the Project Manager will actively seek further comments from interested organisations and individuals.

International Accounting Standard

23. As the final stage of the project, the Steering Committee and the Board will reconsider the proposals in the Exposure Draft in the light of comments on the Exposure Draft. The Steering Committee will approve the final International Accounting Standard for submission to the Board for approval. On the assumption that the comments generally support the Exposure Draft, this stage of the project will take four to six months from the comment deadline. It will require one meeting of the Steering Committee.

Revisions to Work Programme and Timetable

24. This timetable has been prepared on a reasonably optimistic basis, although, in practice, projects take longer to complete than planned for two reasons. First, it is dealing with accounting issues that have not been dealt with, to any great extent, by national standard setting bodies. Secondly, the level of implementation guidance required in the proposed Standard may be greater than is usually the case. There is also a real possibility that the project will result in more than one International Accounting Standard which may lengthen the process.
25. The Board reviews progress on all its projects and their expected timetables at each IASC meeting.

**Resources**

26. The project will be managed by a Project Manager who is a full time member of the IASC staff and who would be expected to spend 75% of his/her time on the project during its initial stages. The Project Manager may be one of the current staff or may be appointed, possibly on secondment from another organisation, to deal with this project. The Project Manager will report to the Technical Director.
27. In view of the nature of this project and the geographical diversity of the issues, the Project Manager will be assisted by Research Assistants who will identify accounting issues, possible solutions and implementation issues by region. Research Assistants will be appointed from developing countries in South East Asia, South Asia, Middle East, East/Central and Southern Africa, West Africa, Caribbean and Latin America. They will spend up to one month on the project in its initial stages. Developed countries will be dealt with by the Project Manager. The Research Assistants will report to the Project Manager.

**Budget**

28. The attached budget has been prepared on the basis of the timetable and work plan. Staff costs are based on estimated salaries, national insurance, pension contribution, relocation costs and other benefits. Travel costs are based on IASC's normal rules for expense reimbursement and assume some savings will be achieved by combining certain trips. Steering Committee expenses assume the IASC will reimburse the travel expenses of five members of the Committee, four of whom are based outside Europe.

**Source:** - Presented to and adopted by the IASC Board  
June 1994

Also attached as Appendix 1 to Agenda Paper 9 *Agriculture – Point Outline*  
for the IASC Board Meeting, Brussels, March 1996  
(Full text of Agenda Paper 9 in Appendix 7B)

## Appendix 7B: IASC Agriculture - Point Outline

NOT FOR RELEASE TO THE  
PUBLIC OR THE PRESS

IASC BOARD MEETING  
BRUSSELS - MARCH 1996  
AGENDA PAPER 9

### Agriculture - Point Outline

#### Introduction

1. The Board agreed in June 1994 to add to its work programme a project which will deal with the recognition, measurement and disclosure of assets, liabilities, income and expenses resulting from growing crops, plantations and forestry, and livestock. The project proposal is attached as Appendix 1.
2. The significance of agriculture, the exclusion of agricultural activities from the ambit of several existing International Accounting Standards, and the diversity of practice found in accounting for agricultural activities, combine to support the need for a Standard on Agriculture.
3. The Board approved membership of the Steering Committee at its November 1994 meeting. Membership of the Steering Committee now comprises:

Canada	Mr H D Howarth ( <i>Chairman</i> )
India	Mr N P Sarda
New Zealand	Ms B A Monopoli
Thailand	Professor K Narongdej
	Dr A Priebjrivat
Zimbabwe	Mr J A Atkinson
France	Mr J Allimant
The World Bank	Mr G Russell (Observer)
Project Manager	Mr I F Kirton

4. The Steering Committee has held two meetings:
  - 18/19 May 1995, London. The main topic under discussion at this meeting was sector scope.
  - 9/10, November Wellington, New Zealand. The main topic under discussion was conceptual scope.
5. Research has been initiated through a questionnaire addressed to IASC member bodies designed to discern:
  - current and recent activity by IASC member bodies in developing promulgations to provide guidance in the accounting and reporting for agriculture producers;

- member body promulgations in existence to guide members involved in the preparation of financial information about agricultural production entities;
- the extent of the exclusion of activities associated with agriculture production entities from existing promulgations;
- agencies with overview responsibilities for agriculture who may have an interest in the development of an accounting standard for agriculture;
- Stock Exchange listed corporations or other reporting enterprises with significant activities in the agricultural production sector; and
- specific issues which the member body believes should be considered in IASC-Agriculture.

A summary of responses to date is attached as Appendix II.

6. Ongoing research is being undertaken into:
- the diversity in accounting and reporting practice for agriculture;
  - the degree of departure from historical cost in the financial statements of agricultural reporting entities; and
  - the means of ensuring the involvement of preparers and users in the due process.

#### **Outline of the Issues**

7. The Steering Committee from the outset acknowledged the delicate balance between the IASC's objectives of improvement and harmonisation, and the genesis of this Point Outline which is sector uniqueness. The Steering Committee is seeking to establish a logic which flows from special industry characteristics, through accounting model selection, to the development of an accounting standard. Where possible recommendations should be fitted into existing IASC *Framework for the Preparation of Financial Statements* (Framework) and Standard structures.
8. The IASC Framework limits applicability to general purpose financial statements (paragraph 6) and therefore, the common needs of users are assumed. In developing accounting policies for a specific entity or sector the special needs of users, both as a consequence of the type of entity, and also the mix of users, need to be considered. The Steering Committee is, therefore, looking to capture the specific needs of general purpose financial statements for agricultural activities.
9. The Steering Committee acknowledges the IASC requirement that the development of standards should be guided by the Framework and therefore, initially focused upon the scope offered by this Framework rather than the constraints of any particular accounting model embedded within existing standards. In this respect the development

of an accounting standard for agriculture has already raised a number of questions with regard to the scope offered by, and interpretation of, the framework, particularly:

- the criteria by which a particular model should be selected;
- a valid range of models;
- the pervasiveness or primacy of a chosen model;
- articulation between alternative models and existing standards; and
- disclosure requirements particularly with reference to the logic of accounting model (for example, dominant activity, stakeholder and regulatory characteristics) and significance of departure from the 'benchmark' accounting model.

10. Issues which the Steering Committee has considered in developing a Standard on Agriculture and for which it seeks confirmation from the Board:

- Objectives
- Sector Characterisation
- Conceptual Approach
- Scope
- Framework - Objectives
- Framework - Underlying Assumptions
- Framework - Elements
- Framework - Recognition

11. Consequential issues which the Steering Committee, and IASC member bodies surveyed, believe should be considered in developing a Standard on Agriculture:

- Framework - Measurement
- Framework - concepts of Capital and Capital Maintenance
- Classification
- Other issues of significance

#### **Timetable for the Project**

12. A timetable for completion of this project is set out below. The Steering Committee in adopting a conceptual approach recognised the practical constraints of such a timetable. The timetable has been prepared on a conservative basis but timing could be influenced by a number of factors, for example, emergence of new issues, increased co-operation with member bodies currently active in the area, or intransigent conceptual stances.

Timing	Milestone
May 1995	Steering Committee meeting to develop initial scope.
November 1995	Steering Committee meeting to develop draft Point Outline.
March 1996	Point Outline discussed by Consultative Group and approved by Board.
May 1996	Steering Committee meeting to develop Draft Statement of Principles (DSOP).
October 1996	Steering Committee meeting to approve DSOP.
November 1996	DSOP issued for comment by 28 February 1997.
April 1997	Steering Committee meeting to approve Statement of Principles (SOP)
June 1997	Board to approve SOP.
August 1997	Steering Committee meeting to approve draft Exposure Draft for submission to the Board.
October 1997	Exposure Draft discussed with Consultative Group and approved by Board.
December 1997	Exposure Draft issued for comment by 30 June 1998.
October 1998	Steering Committee meeting to consider comments and to approve draft International Accounting Standard
November 1998	Board to discuss draft International Accounting Standard
March 1999	Board to approve International Accounting Standard.
April 1999	International Accounting Standard issued, effective January 2000

### Objectives

13. The objective of this project is to research and draft for the approval of the IASC Board an International Accounting Standard on agriculture which will improve the relevance and reliability of published financial statements of enterprises involved in agriculture.
14. To achieve this objective the Steering Committee will:
  - consider the relevance of existing International Accounting Standards to agricultural activities and, in particular, address existing exemptions;
  - consider the need for an additional International Standard for agricultural activities;
  - review the impact of conceptual issues discussed by the Steering Committee during the project and to recommend to the Board, if necessary, any revisions or developments to the framework; and

- illustrate any recommended accounting and disclosure treatments by way of specific examples designed to broaden application beyond those reporting enterprises required to prepare general financial statements.

### **Sector Characterisation**

15. The economic significance of the agricultural sector is well documented in both developing and developed economics. Significance alone, however, is insufficient to warrant a specific standard. The Steering Committee recognised that by excluding agriculture from the scope of a number of accounting standards (e.g. IAS, Sri Lanka, Australia), accounting standard setters were signalling a fundamental difference in the nature, and activities of agriculture.
16. In order to clarify the nature and activities of the sector the Steering Committee proposes that agriculture should be defined as the *"Management of the biological transformation of animal and plant, to produce products for consumption or further processing"*. The Steering Committee believes that expansion of the components of this definition further clarifies the subject of this standard.
17. **Biological**
  - Relating to life phenomena. The animal and plant components of an agriculture system have a life of their own capable of growth (including procreation and change in form) without human intervention. Such life is generally dependent upon a combination of natural resources i.e. sunlight, water, air, and soil.
18. **Transformation**
  - A change in quality (e.g. genetic merit, density, ripeness, fat cover, protein content, fibre strength) and /or quantity (e.g. progeny, live weight, cubic metres, fibre length/diameter, stems, buds, suckers, deaths, losses) over a period of time; and
  - is monitored and measured as part of management control, such measurement is becoming increasingly objective (e.g. weighing, laboratory analysis, girth measurement).
19. **Managed Process**
  - Management attempts to facilitate the biological transformation by enhancing or stabilising conditions necessary for the process to take place (e.g. nutrient levels of the growing medium, soil moisture, temperature, sterility, fertility, immunity, light);
  - control exerted over the conditions (intensive cf. extensive) determines the relationship between human intervention (with associated costs) and production. The less control, the more tenuous the relationship; and



- differentiates agriculture from exploitation in the form of extraction (e.g. fishing, clear felling, mining) which makes no attempt to facilitate the transformation. Extraction or harvest is an essential part of agriculture but alone does not constitute agriculture.

20. **Products**

- of agriculture are diverse and generally require further processing before ultimate consumption;
- management often has a choice of product from an animal or plant species (e.g. forestry-clearwood, pulp, roundwood firewood, or any combination, sheep-wool, meat, progeny for replacement); and
- the coincidence of, a combination of product from a species; a combination of species; and a tenuous relationship between human intervention and product, create difficulties in cost attachment to product.

21. **Consumption and/or further processing**

- Agricultural products serve to satisfy two of the basic needs of human beings, i.e. food and shelter;
- depending upon the state of maturity of an economy, agriculture assumes a developmental role brought into play by lengthening the value chain, from subsistence to self sufficiency, from self sufficiency to export significance;
- the importance of the products of agriculture to satisfy basic needs often give rise to government intervention to ensure adequacy of supply (production) and accessibility (pricing); and
- the agricultural producer is often one of a number of producers, not seen to be in competition, co-operating on a regional or national basis to add further value to product (Co-operatives).

22. The Steering Committee believes biological transformation, the innate ability of biological assets, is the source of sector uniqueness.

23. The Steering Committee noted that the majority of promulgations developed by member bodies were for biological assets with longer production cycles (e.g. plantations, forestry, livestock). The significance of time to maturity or marketability can be significant within a transaction based accounting model as there is a greater potential for transaction based costs to deviate from market derived values. The Steering Committee considered that whilst the length of time highlighted the divergence, the potential for divergence was present in all agricultural production systems. Such a view was also sustained when considering interim reporting, or any situation where the production cycle and accounting cycle do not coincide.

24. The Steering Committee acknowledges that difficulties surrounding accounting for agriculture are compounded by a number of other significant features of agriculture, for example:

- large numbers of small production units with no requirement to produce general purpose financial statements and with a basic tax or cash orientation;
- product processing and input acquisition often facilitated by co-operative membership;
- government intervention in production and pricing decisions; and
- joint products and joint costs often confound cost relationships.

However, the Steering Committee considered that these features individually are neither unique to agriculture nor are present in all agricultural systems.

25. The Steering Committee identified a diverse range of agricultural systems, brought about by; the vast array of plant and animal species; the potential for species to generate alternate or joint products; and the capability of combining species in mixed systems. The definition adopted by the Steering Committee embraces products as diverse as rubber, tea, sugar, timber, eggs, salmon, prawns, deer velvet, fibre, annual flowers and vegetables.

26. The Steering Committee will be striving to develop a Standard applicable to all agricultural systems and in particular all biological assets. In existing member body guidelines a number of taxonomies are used to subdivide the biological asset group (for example, maturity, life cycle, pattern of production [consumable or bearer] or, plant or animal). The Steering Committee will consider the significance of such taxonomies in relation to the dominant feature, that is, transformative capability and the need for specific classification or additional sub-classification.

27. The diversity of agricultural system is compounded when environmental, economic and regulatory conditions are overlaid. Such diversity suggests caution in inferring homogeneity with regard to risk and return for agricultural producers. The Steering Committee will consider the application of ED51, Reporting Financial Information by Segment, to entities undertaking agricultural production activities with significantly different risk/return characteristics.

#### **Conceptual Approach**

28. The IASC Framework purports to be applicable to a range of accounting models. The conceptual dilemma which confronted the Steering Committee was whether to:

- seek possible solutions in terms of the most appropriate accounting model available; or
- seek possible solutions in terms of the most common and accepted accounting model.

29. The Steering Committee therefore:

- a) considered sector characteristics and user needs, and tested the relevance and reliability of alternate 'pure'

accounting models for a range of agricultural activities. This approach was seen to:

- be consistent with both the Framework and the project brief (interpreted as developing an accounting Standard for the activities of agriculture);
- provide the preparer with a clear conceptual model with attached meanings by which a measurement system could be applied; and
- provide the user with the assurance that the financial statements are internally consistent and have a specific meaning in terms of the accounting model chosen.

Alternative models considered were:

- transaction based/historical cost;
  - value based/value in use; and
  - value based/value in exchange.
- b) considered relaxing the pure historical cost accounting model to allow revaluations for specific agricultural assets. The modified historical cost approach is consistent with existing Standards.

30. The Steering Committee reached the conclusion that:

- there is an urgent need for harmonisation of existing accounting practice;
- there is limited guidance available within the Framework for a departure from transaction based accounting models;
- the time frame required to develop a value-based model is considerable and the repercussions such as to take this approach beyond the scope of the project;
- discussion should be limited to recognition and measurement of biological transformation;
- precedents in existing Standards provide a useful starting point; and
- a review of the impact of conceptual issues discussed during the course of the project should be undertaken and recommendations for further development or clarification of the Framework should be made to the Board.

31. The Steering Committee proposes that:
- a modified historical cost approach should be adopted;
  - the assets for which modification will be considered should be those biological assets unique to agriculture; and
  - guidance should be provided for elements not falling within the biological asset classification, yet significant to agriculture, drawing upon the requirements specified in, and flexibility offered by, existing Standards.
32. The Steering Committee recognises that the proposed approach now more closely aligns this project with that being undertaken by the Australian Accounting Research Foundation in their project *Accounting for Self-generating and Regenerating Assets*. The Steering Committee will strive to ensure a synergy between the two projects.

#### Scope

33. The Steering Committee believes the proposed Standard should apply to general purpose external financial statements of enterprises with agricultural activities.
34. The Steering Committee observed that many of the guidelines developed by member bodies targeted user groups not required to prepare general purpose external financial statements. The Steering Committee is optimistic that use will extend to such groups due to the universality and clarity of the proposed standard, and the simplicity and explanatory power of the proposed accompanying illustrations.

#### Framework-Objectives

35. The Framework (paragraph 110) and Draft Statement of Principle "*Presentation of Financial Statements*" (Principle 18) identify that choice of an accounting model or an accounting policy should be on the basis of relevance and reliability.
36. The Steering Committee considered the information needs of three main groups of external user.

#### Investors

The IASC Framework identifies that investors are concerned with the risk inherent in, and return provided by, their investments. The general acknowledgement of inherent business risk in agricultural activities cautions investors to seek returns commensurate with the level of risk.

#### Lenders

Agriculture is an activity which:

- often requires considerable investment in long-lived assets relative to total assets (particularly where land, development or time to maturity is involved);

- due to seasonality, often requires short term operational finance. The large numbers of agricultural entities requiring high levels of investment and Government encouragement to invest, have often led to levels of debt which generally would not be considered prudent given the high business risk. Lenders will be interested in information enabling assessment of financial risk. Whilst banks have detail information derived from monitoring of daily cash flows, and specific information required as a condition of borrowing, periodic affirmation is required.

### **Governments and their agencies**

There is a considerable history of government intervention in the production and pricing of agricultural production. Agriculture has been viewed as an essential industry in terms of the products it supplies (satisfying two basic human needs of food and shelter) and hence prompting measures to ensure adequacy of supply (production) and access to supply (pricing). Once basic needs are met agriculture is seen as a means of initiating economic development. The protections instituted for the former and the importance attached to the latter often combine to lead to a dependence upon continued intervention. Government and their agencies need information to monitor the effectiveness of interventions in delivering desired outcomes.

37. The Framework acknowledges three different but overlapping purposes for financial statements.
- a) Decision usefulness. By considering the needs of significant users of financial information, and the specific decisions implied by accountability and stewardship, the Steering Committee is confident the decision usefulness objective of financial statements will be met.
  - b) Accountability. The Steering Committee defined accountability as the reconciliation of actions taken and resultant position with prior statements of intent which have formed the basis of stakeholder expectation. The Steering Committee is aware of increasing enunciation of intent, for example

*Tasman Agriculture's focus will be to continue to increase shareholders' assets by conversion arbitrage - adding value to sheep and beef grazing land by converting it to dairying.*

*... to spread risk by commodity and geographical location so that realised profits may be in the order of 30% cotton, 30% horticulture, 20% wine grapes, 20% cereal, wool and eating sunflower.*

The Steering Committee will therefore be considering the need to weigh such statements of organisational intent when considering the events to be recognised and the measurement of the events in the financial statements.

- c) Stewardship. The Steering Committee acknowledges the need for information which will facilitate judgements regarding distributions made and compliance with legal obligations which are the primary focus of the transaction based/historical cost model. The Steering Committee is aware that any modifications to this model, particularly in

terms of non-transactional events recognised, will need to ensure that concepts of capital and capital maintenance, and disclosures, enable such judgements to be made.

38. The Steering Committee is of the opinion that biological transformation is the unique event which distinguishes agricultural activities from other activities. Resources are marshalled toward facilitating and sustaining growth, an activity specifically entered into to change the substance of assets in a way which enhances value of the asset.
39. The Steering Committee concurs with the view that the essence of reliability is the degree of correspondence between what the information conveys to statement users and the underlying transactions and events that have occurred and have been measured and displayed. Existing Standards formulated in relation to a transaction based/historical cost model:
- often exclude from their scope specific agricultural activities;
  - give rise to a diversity of accounting practice; and
  - are often in conflict with guidelines developed by user groups.

Such observations have been interpreted by the Steering Committee as evidence that this 'pure' model does not adequately capture the events impacting upon agricultural activities.

40. In many agricultural activities, particularly the more extensive, there is an indirect relationship between transactions and biological transformation. The Steering Committee is of the opinion that transaction based recognition and measurement methods can:
- provide only a partial portrayal of such activities; and
  - introduce bias by excluding a material event.

#### **Framework - Underlying assumptions**

41. Accrual assures the user that significant transactions and events are recorded and recognised in the financial statements in the periods in which they have occurred and not as cash or its equivalent is received or paid. The Steering Committee in acknowledging the significance of biological transformation within agricultural entities will need to ensure, subject to the asset meeting the definitional and recognition requirements specified in the Framework:
- that the measurement system can capture the substance of entity activities to enable periodic recognition of such transactions or events; and
  - that the measurement system has adequate gradations to sensitively portray the between period changes in this substance.

42. The Steering Committee will carefully consider the relationship of going concern to sustainability of agricultural activities. The Steering Committee has tentatively concluded that sustainability exists in the context of biological assets when output levels are maintained either through evidenced ongoing replacement programmes (bearer systems) or existence of multiple generations (consumable systems). A limited life production system might grow to maturity one generation of animal, or tree crop. The Steering Committee believe the distinction may be important:
- for long production cycle systems where "foreseeable future" becomes ambiguous; and
  - in providing, in the absence of clear recommendation within the Framework, some guidance for preparers of financial reports for agricultural activities where going concern is clearly violated.
43. The Steering Committee will consider the relevance of developments in accounting for environmental assets and liabilities. The dependence of agricultural production systems upon, and the ability of such systems to deplete, natural resources, indicates that the measurement and disclosure of critical qualities could be particularly pertinent in going concern or sustainability decisions.

#### **Framework - Elements**

44. In the Steering Committee's opinion biological resources are tangible resources controlled by an enterprise from which future benefits are expected to flow to the enterprise and, therefore, conform to the Framework definition of an asset. The Framework specifically identifies that:
- events other than transactions may generate assets (para 58); and
  - the absence of a related expenditure does not preclude an item from satisfying the definition of an asset (para 59).
45. The definition of income and expense in terms of period changes in assets and liabilities (para 70) means that there appears to be no obstacle to an event resulting in a change in an item defined as an asset or liability moving to the recognition criteria.
46. In research to date the Steering Committee has found no disagreement with the classification of biological resources as assets.

#### **Framework - Recognition**

47. The Steering Committee considered whether biological assets as a whole, or a subset of such assets, should be formally recognised in the financial statements of an entity, by token of meeting the two recognition criteria:
- it is probable any future economic benefit will flow to or from the enterprise;
  - the item has a cost or value that can be measured with reliability.

48. The Steering Committee considered that the agricultural enterprise is founded on the assumption that benefits will flow from biological assets as they are the primary source of economic benefit. To challenge the certainty of flow is to challenge the assumption of going concern.
49. Biological assets are tangible. The characteristics which give rise to the ability to generate economic benefits are measurable and can be related to the qualities valued by the market. In the Steering Committee's opinion there generally exists both a cost and value. Whilst the Steering Committee identifies that there is generally both a cost and value they also note the Framework acknowledges *the use of reasonable estimates is an essential part of the preparation of financial statements*.
50. In research to date the Steering Committee has found no disagreement with the recognition of biological assets.

#### **Framework - Measurement**

51. The Steering Committee believes that to select an accounting policy for biological assets which conforms to the Framework requirements of relevance and reliability, the biological growth event must be recognised.
52. Historical cost measurement of such assets recognises the assets but not biological growth. The Steering Committee believes that other transaction based measurement methods, for example compounded historical cost or cost of replacement through normal course of business, will demonstrate the same deficiency.
53. In adopting a modified historical cost approach the Steering Committee will need to take cognizance of existing Standards and current developments which allow or are considering departures from historical cost valuations, for example, IAS 16, Property, Plant and Equipment, IAS 25, Accounting for Investments, and Phase II Financial Instruments. In addition to the precedents sought for the measurement method the Steering Committee will need to consider guidance available for consequential issues such as income tax effects, depreciation, treatment of non-biological movements in value, presentation and disclosure.
54. The Steering Committee will consider identifying an overall benchmark for the measurement of all biological assets. Pertinent to such considerations are:
- a) Identification of alternate measurement methods
    - The Steering Committee is currently considering both market based (exit or entry) and expectation based (NPV) measurement methods;
    - precedent exists for *fair value usually market* (IAS 16);
    - there exists within current Standards a presumption that such measures are available and in use, for example, periodic assessment of whether recoverable amount is below the carrying amount of fixed assets (IAS 16) or the



measurement of inventories at the lower of cost and net realisable value (IAS 2).

- b) The applicability to all biological assets
    - A proposed benchmark will need to be tested on a range of biological assets in a range of locations giving due consideration to features such as:
      - maturity - mature/immature
      - species - plant/animal
      - production - bearer/consumable
      - life cycle - short/long
      - management - sustainable/limited life
  - c) In the absence of the primary benchmark are surrogates available.
  - d) The consequential impact on revenue recognition when biological assets are harvested.
    - IAS 2 excludes *producers' inventories of livestock, agricultural and forest products ... to the extent that they are measured at net realisable value in accordance with well established practices.*
  - e) The depth and sensitivity of markets for biological assets.
  - f) The appropriate market from which market price should be sourced.
    - IAS 16 describes fair value of land and buildings as usually its market value for existing use, and for items of plant and equipment as usually their market value determined by appraisal. Biological assets will often have a value based upon intended use as well as existing state, for example immature trees suitable for pulpwood but managed for clearwood.
55. The Steering Committee is aware that biological transformation is just one of several variables captured within a market valuation. In the context of a modified historical cost approach treatment of value increments attributable to other factors, for example general and specific price changes, would need to be consistent with either application of the historical cost accounting model or precedents established within existing Standards. The Steering Committee will attempt to reconcile such requirements with the Framework criteria of relevance and reliability.
56. Where assets of significance to agriculture (particularly land, possible also riparian rights, quotas) have available a benchmark and allowed alternative treatment, the Steering Committee will consider whether a preferred treatment should be expressed consistent with the recommended treatment for biological assets.

### Framework - Capital and Capital Maintenance

57. The Steering Committee will review the relationship between an accounting model and the application of a concept of capital and capital maintenance. The Steering Committee is initially of the view that in adopting a modified historical cost approach concepts of capital will be sourced from the historical cost accounting model, i.e. a financial concept of capital.
58. The Framework provides insight into the concept of financial capital maintenance where capital is defined in terms of nominal monetary units by stating that whilst increases in the prices of assets held over a period are conceptually profits they may not be recognised until the assets are disposed of in an exchange transaction. This view appears consistent with the treatment of revaluations of property, plant and equipment described in IAS 16.
59. The Steering Committee will test the decision usefulness of this interpretation in the context of agricultural systems.

### Asset Classification

60. The Steering Committee has identified that biological assets have a unique characteristic. Pertinent to interpretation of existing Standards is the classification of such assets. The Steering Committee will be considering several alternatives, including:
- a separate classification of assets (for example, biological, or self-generating and regenerating assets) capable in itself of being sub-classified (for example, mature/immature and/or bearer/consumable); and
  - preservation of the dichotomy which exists in current Standards relating to tangible assets, and classification as either inventory or fixed assets.
61. The Steering Committee will consider whether by proposing that the transformative attributes of biological assets should be recognised (growth as an event which confers economic benefit) it is attributing to biological assets, whether mature or immature, qualities more associated with fixed assets than inventory. Such reasoning would:
- clearly delineate between biological assets and the product of biological assets (having the character of inventory);
  - enable some consistency in treatment of other assets necessary for the production process, particularly land, where allowed alternative treatments are available and used; and
  - would increase the potential for one proposed measurement method to apply to all biological assets.

**Depreciation/Diminution**  
**Structure and Content of Financial Statements**  
**Notes to the Financial Statements**  
**Other Disclosures**  
**Segmental Reporting**  
**Subsidies and other interventions**  
**Co-operatives**  
**Taxation**

62. The Steering Committee acknowledges that the above issues are of significance but not unique to agriculture. A review of existing Standards and work in progress will be undertaken to ascertain whether specific guidelines need to be incorporated within a Standard on Agriculture or whether the implementation guidelines the Steering Committee intends to produce should be structured to illustrate an interpretation of existing Standards in relation to these issues.

**Appendix 8A: IASC Board Delegates & Technical Advisers**

AGENDA PHASES		ED	ED 83	Standard
DELEGATIONS	MEMBERS	1998	1999	2000
Australia	Kenneth Spencer <sup>100</sup>	x	x	x
	David Boymal	x	x	
	Ian Hammond			x
	Brian Morris			x
Canadian	Alex Milburn	x		
	James Gaa	x	x	x
	Paul Cheery		x	x
French	Gilbert Gélard	x	x	x
	Jean Keller	x	x	x
German	Bernd-Joachim Menn	x		
	Jochen Pape	x	x	x
	Helmut Berndt		x	x
Japanese	Tatsumi Yamada	x	x	x
	Shozo Yamazaki	x	x	x
Mexican	Luis Moirón Llosa	x	x	x
Netherlands	Jan Klassen	x	x	x
	Jan den Hoed	x	x	x
United Kingdom	Christopher Nobes	x	x	x
	Sir David Tweedie	x	x	x
United States	Michael Crooch	x	x	x
	Mitchell Danaher	x	x	x
	John Smith			Oct-Dec
South African	Erna Swart	x	x	
International Council of Investment Assns.	Rolf Rundfelt	x	x	x
	Patricia McConnell	x	x	x
	Nobuaki Kemmochi	x		
	Toshihikio Amano <sup>101</sup>		x	x

# ED 83 Submission Signatory

<sup>100</sup> Support ED 83, with drafting changes.<sup>101</sup> Support ED 83 in principle.

<b>AGENDA PHASES</b>		<b>ED</b>	<b>ED 83</b>	<b>Standard</b>
<b>DELEGATIONS</b>	<b>MEMBERS</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>
Fedn. Swiss Holding Companies	Harry Schmid Peter Zurbrügg Malcolm Cheetham	x x	x  x	x  x
IFAC	Thomas Jones David Potter <sup>102</sup> Luis Nelson Carvalho Martin Noordzil	x x	x x x x	x x x x
Nordic Fedn. of Public Accountants	Erik Mamelund Stig Enevoldsen Sigvard Heurdin Per Gunslev <sup>103</sup>	x x x x	x x x x	x x x x
Indian/Sri Lankan	Reyaz Mihular Thekkiam Sitaram Vishwanath Narian Dass Gupta	x x	x x	x x x
Malaysian	Tony Seah Cheoh Wah Katharene Expedit <sup>104</sup>	x	x	x x

**Agenda Phases:****ED****Exposure Draft E65 – Issued - July 1999****Standard****IAS 41 Approved – December 2000**

# ED 83 Submission Signatory

<sup>102</sup> Support in principle; but need a Field Test for practicality & reliability, plus G4+1 work on reporting FV changes in Income Statement or permitting cycling on realisation.

<sup>103</sup> Support in principle, but with reservations with further work required.

<sup>104</sup> Not full support. In particular, on reliability of FV measurement and valuation for bearer biological assets.

AGENDA PHASES		ED	ED 83	Standard
DELEGATIONS	TECHNICAL ADVISERS	1998	1999	2000
Australian	Warren McGregor Jan McCahey Angus Thomson	x x	x  x	  x
Canadian	Robert Rutherford <sup>105</sup>	x	x	x
French	Annie Moutardier-Mersereau Christophe Patrier	x	x x	 x
German	Albrecht Ruppel Klaus-Peter Naumann <sup>106</sup>	x x	x x	 x
Japanese	Etsuo Sawa	x	x	
Mexican	Carlos Buenfil	x	x	x
Netherlands	Cees Dubbeld Ruud Vergoossen	x x	x x	x x
United Kingdom	David Perry	x	x	x
United States	Elizabeth Fender <sup>107</sup> Fred Gill	x x	x x	x
South African	Leslie Anderson Erna Swart <sup>108</sup>	x	x	x x
International Council of Investment Assns	Patricia McQueen	x	x	x
Fedn Swiss Holding Companies	Philipp Hallauer <sup>109</sup>	x	x	x

**Source:** Appendix 3 Camffermann and Zeff (2007, pp. 506-12 )

# ED 83 Submission Signatory

<sup>105</sup> Not support. The case for FV accounting for agriculture has not been made sufficiently.

<sup>106</sup> Not support. Inconsistent with IAS 40 FV principles nor in favour of applying FV to non-monetary assets.

<sup>107</sup> Disagrees with E65 basic principles biological assets should be valued and measured at FV; Historic Cost (HC) mostly more appropriate.

<sup>108</sup> Not support. Should permit choice between HC and FV; no support for solely FV.

<sup>109</sup> *Inter alia*, doubts on FV reliability; needs Field Test; disagrees with FV changes to Income Statement; inconsistent with IAS 39 principles.

### **Appendix 8B: IASC Agriculture Steering Committee (SC) Membership**

(Indicative dates)

AGENDA PHASES		PO	PO	PO	DSOP	DSOP ED	ED	FTP /Std
MEMBERS		1994	1995	1996	1997	1998	1999	2000
P. Dumont	France	M	M					
J. Allimant	France			M	M	M	M	M
N.P. Sarda	India	C	C	M	M			
H Horwath	Canada		C	C				
J. van Ham	Netherlands							
Ms B. Monopoli	NZ	M	M	M	M	M	M	M
M. Reyaz Milhular	Sri Lanka				C	C	C	C
K. Narongdej	Thailand	M	M	M				
A. Priebrivat	Thailand			M	M	M	M	M
S. Dedman	UK					?	?	M
J.A. Atkinson	Zimbabwe	M	M	M	M	M	O	O
G. Russell	World Bank	M	M	O	O	O	O	O
R. Keys	AASB							O
<b>PROJECT MGRS</b>								
I. Kirton	NZ		PM	PM	PM			
P. Pacter	IASC					PM	PM	
Ms R. Yanou	Japan							PM

**Agenda Phases:**

<b>PO</b>	<b>Point Outline – Prepared March 1996</b>
<b>DSOP</b>	<b>Draft Statement of Principles – Issued December 1996</b>
<b>ED</b>	<b>Exposure Draft E65 – Issued -. July 1999</b>
<b>FTP</b>	<b>Field Test Project – Issued – March 2000</b>
<b>Std</b>	<b>IAS 41 Approved – December 2000</b>

**Steering Committee Members:** (N.B. Indicative dates)

<b>PM</b>	<b>Project Manager</b>
<b>C</b>	<b>Chairman</b>
<b>M</b>	<b>Member</b>
<b>O</b>	<b>Observer</b>

**Source:** (Camfferman and Zeff, 2007)

## **Appendix 9: DP 23 Special Topics**

### **1. Measurement of SGARAs**

DP 23 measurement alternatives were segregated between the forests and livestock archetypes and can be summarised at a high level between:

**Cost** - Sn. 4.4.1 (pp. 30-7); and Other - Sn 6 (pp.121-4)

This was further subdivided into alternative cost methodologies being

a) Historical Cost	<b>Forests</b>	Sn. 4.4.1(a) (pp. 31-6) and
	<b>Livestock</b>	Sn. 4.8.1(a) (pp. 54-9)
b) Compound Historical Cost	<b>Forests</b>	Sn. 4.4.1(b) (pp. 36-7)
c) Replacement Cost	<b>Forests</b>	Sn. 4.4.1(c) (p. 37)
d) Cost based on Income Tax legislation	<b>Livestock</b>	Sn. 4.8.1(b)
e) Cost based on Market Value	<b>Livestock</b>	Sn. 4.8.1(c) (p. 60)

**Value – Forests** - Sn. 4.4.2 (pp. 37-50); and Other - Chap. 6 (pp. 73-81)

Subdivided into the valuation methodologies (pp. 39-50) for:

a) Net Present Value (NPV)	<b>Forests</b>	Sn. 4.4.2
b) Current Market Value (CMV)	<b>Forests</b>	Sn. 4.4.2(b)

**Forest and Livestock CMV** was further subdivided for discussion purposes into:

Exit vs. Entry Prices for	<b>Forests</b>	(pp. 46-50)
Deprival Value Model		Appendix 5 (pp. 117-19)
Current Market Value	<b>Livestock</b>	Sn. 4.8.2(a) (pp. 60-2)
Discounted Market Value	<b>Livestock</b>	Sn. 4.8.2(b) (p. 62)
Standard Value	<b>Livestock</b>	Sn. 4.8.2(c) (p. 62-3)

**Artificial Cost and Value Price Schedules** **Forests** Sn. 4.4.3 (pp. 50-1)

### **Source:**

Discussion Paper No. 23, *Accounting for Self-Generating and Regenerating Assets*; Roberts *et al.*, 1995



## 2. DP 23:- Consideration of Other non- forestry and livestock Sectors

DP 23 provided a survey of financial practices adopted by Other SGARA industries (Roberts *et al.*, 1995, Appendix 6). It supplied commentary on the assumed applicability of transferring the DP 23 proposed forestry and livestock accounting for each sector:-

### A. Consumable Crops.

DP 23 discussion covered field and row crops, *i.e.* grain, agri-industrial and vegetable categories, perennial crops and sugar cane crops. After reviewing current practice, essentially from a cost-centred perspective, it concluded:

based on the limited research into SGARAs relating to consumable crops conducted for the purpose of this Paper, the financial reporting issues associated with SGARAs related to consumable crops are fundamentally similar to those facing forestry and livestock SGARAs. Accordingly, the recommendations made earlier in this Paper are, in principle, applicable to consumable crops. However it is acknowledged that the recommendations relating to asset measurement and revenue recognition and measurement should only be adopted where the benefits outweigh the costs of implementing the recommendations. A factor which should be considered in such a cost/benefit analysis is the length of the production cycle of consumable crops. A review of all the costs and benefits associated with adopting the recommendations made in this Paper for consumable crops is beyond the scope of this Paper. However, where the economic life of a consumable crop is short and therefore the time between when it might be valued for financial reporting purposes and when it might be sold is short, it may be reasonable to wait until the output of the crop is sold to recognise any value attributable to growth as revenue. As such it may be appropriate, based on pragmatic criteria, to value consumable crops prior to sale using cost-based methods rather than current market value methods (*ibid.*, p. 76).

This commentary is reproduced in full. There are a number of features. Absent was the certainty – without further research – as to whether current value accounting was appropriate; for that, a cost/benefit analysis was required. Pragmatically, DP 23 noted valuation prior to sale may be considered more appropriate using cost-based methods.

There is no evidence any further research or cost/benefit analysis occurred. Subsequently, within the IASC, the variability in valuation bases at point of harvest, or at any reporting date due to external factors, was a continuing point of difference and debate.

### B. Fruit Bearers: Orchards and Vineyards.

Given the DP 23 biological taxonomy emphasis, and insufficient analysis about economic functionality differences between bearer and consumable SGARA, the discussion for this agricultural sector confused the issue further by attributing asset-life longevity as the appropriate Bearer comparator to a forest asset.

DP 23 stated:

the growing stock of a grapevine can be over a hundred years old and so potentially approximates the forest as a very long-lived SGARA (*ibid.*, p. 76)...(and)

notwithstanding the difference in functionality, DP 23 concluded:

similar to the conclusion drawn for consumable crops – *i.e.* lack of certainty about current value accounting, need for a cost/benefit analysis and cost-based models prior to sale, the financial reporting issues associated with Fruit Bearers are, in principle, similar to those facing forestry and livestock SGARAs. Accordingly, the issues discussed are applicable to such fruit bearers (*ibid.*, p. 77).

Comment:

Virtually every submission from *bearer*-industry representatives, on ED 83 (Australia) and ED-90 (New Zealand) and also to the AASB's post-evaluation review, revealed sustained disagreement and objections from recording unrealised asset value gains/losses within income. Integrated Wine Companies objected to recording own-harvest at full market value in inventories, and not at cost. This was to cause severe unintended consequences for any listed agricultural sector company which did not recognise the non-cash implications of these unrealised components. This was in direct contrast to the proposals for Stud Breeders below.

The DP 23 conclusions may have occurred because in the original investigation survey only one horticulturist, and no viticulturist or viniculturalist, responded to the request to participate. There was therefore insufficient evidence and no specific research to validate the assumptions summarised above. Moreover many would have been small/medium unlisted/family entities not required to prepare GPFRs anyway.

### **C. Aquaculture and Fishing 'Consumables'**

After discussing physical processes unique to this sector and the commonly used accounting treatment and issues faced by participants, DP 23 concluded:

generally, aquaculture livestock has a short cycle of operations (in fishing even shorter) which does not present as many reporting problems as exist for longer-lived SGARAs such as sheep and cattle.

Most operations attributable to a cycle fall within one financial period. However to the extent that this does not occur, the principles addressed in relation to the financial reporting of forestry and livestock SGARAs appear to have application to aquaculture and fishing consumables. Before adopting such principles for SGARAs relating to aquaculture and fishing consumables, the implications of those principles need to be considered from a cost/benefit perspective. As indicated above, such a cost/benefit analysis is beyond the scope (of DP 23) (*ibid.*, p. 78).

### **D. Short-term Livestock 'Bearers' – for example, Hens"**

The DP 23 discussion concluded:

while these short-term bearers are treated as current assets, they are effectively consumed in production within a year and could therefore be recognised as period production costs.

Once again, although the fundamental nature of short term livestock "bearers" are similar to forestry and livestock SGARAs, the costs and benefits of applying the financial reporting practices proposed to such bearers need to be considered before such practices are adopted. Given the short-term nature of the "livestock" bearers it may be inappropriate to adopt the practices for such SGARAs. This question is beyond the scope of (DP 23) (*ibid.*, p. 79).

**E. Stud Breeders**

This section reviewed Australian practice and the New Zealand Farm Accounting Technical Practice Aids. DP 23 noted TPA No.7 *Accounting for Bloodstock Enterprises* recommended thoroughbreds for sale be treated as current assets valued at cost, whilst breeding or racing horses<sup>110</sup> be treated as non-current assets, valued at written-down cost. DP 23 raised the objection that managerial intent influenced the choice of valuation technique and accounting policies under the New Zealand recommendation.

However, their rationale for adopting cost was:

it was not prudent to revalue thoroughbred bloodstock as any resultant excess would give rise to an unrealised gain, the ultimate realisation of which would be subject to uncertainty given the nature of the assets and the industry.<sup>111</sup>

DP 23 concluded

stud breeders would appear to be different from many of the other SGARA- related industries because their production cycle is not short-term. Given the self-generating nature of stud breeders, they are similar in nature to the livestock industries. Accordingly, (DP 23) recommends that the general principles proposed (for traded livestock) be adopted for stud breeders (*ibid.*, p. 80).

**F. Biotechnology**

Whilst DP 23 noted this was a separate specialised topic, it recognised Biotechnology was a small but rapidly growing industrial process:

whereby artificial intervention is maximised in plant/animal production in an attempt to gain efficiencies of product development.

DP 23 accepted biotechnology posed its own set of problems and controversy for financial reporting...and effectively being a *non-human-related living unit* any such SGARAs possess an economic value which met recognition and reporting criteria, whether short- or long-term. However,

definitional, and perhaps even ethical, problems can be expected to emerge as biotechnological advances lead to new questions such as when the unit can be considered “living” ...(therefore) further research into the financial reporting issues related to biotechnological assets is necessary before concluding on the way on which such assets should be recognised in general purpose financial reports (*ibid.*, p. 87).

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<sup>110</sup> In the eventual Standards racing horses were excluded as not meeting SGARA definitional criteria.

<sup>111</sup> *ibid.*, p. 80; citing Juchau, Clark R.H., M.B.Clark and J.J. Radford, *Agricultural Accounting, Perspectives and Issues*, Lincoln University, N.Z., 1989, pp. 5, 18-19.

## Appendix 10: IASC Draft Statement of Principles (DSOP) and Invitation to Comment

### Introduction

#### **The Need for an International Accounting Standard**

- Q 1** -- *Do you agree that IASC should issue an International Accounting Standard on Agriculture?*
- Q 2** - *Does the Steering Committee's (SC's) characterisation of agriculture conform to your understanding of the sector?*
- Q 3** – *A number of implications flow from the SC's description of agriculture. Do you agree that:*
- a) biological transformation is a significant event that, under an accrual basis of accounting, should be recognised and reported in the period in which it occurs;*
  - b) the effect of changes in substance brought about by biological transformation is best revealed by reference to the changed state of the biological asset;*
  - c) the items to be accounted for should be the class of animals or plants rather than the individual animal or plant; and*
  - d) active and efficient markets generally exist for both biological assets and agricultural produce?.*

### Scope

**Principle 1** – **This statement applies to general purpose financial statements of all enterprises that undertake agricultural activities.**

- Q 4** – *Do you agree that the Principles established can generally be applied to*
- a) all agricultural activities; and*
  - b) agricultural enterprises required to produce general purpose financial statements?*
- Q 5** – *The SC is committed to assessing the need for practical guidelines to accompany a Standard to facilitate wider adoption of recommended accounting principles.*  
*Is there a need for such guidance?*  
*Should such guidance be initiated at the international or national level?*

### Definitions

The following terms are used with the meanings specified

**Agriculture** – is the management of the biological transformation of animals and plants to yield produce for consumption or processing.

**Biological transformation** comprises the events of self-generation, regeneration, and degeneration. These events encompass both a qualitative and quantitative change in the animal or plant and generation of new assets in the form of items of agricultural produce and/or additional biological assets of the same class.

**Biological assets** are living, groups of animal and plant classes held by an enterprise for their biological transformative capabilities.

**Agricultural produce** is the harvested non-living product of an enterprise's biological assets awaiting sale, processing or consumption.

**Fair value** is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

**Carrying amount** is the amount at which an asset is included in the balance sheet after deducting any accumulated depreciation or amortisation thereon.

**Q 6** – *Do the definitions of agriculture, biological transformation, biological assets and agricultural produce clarify the subject and boundary of this DSOP?*

### **Recognition of Biological Assets**

**Principle 2** – Animals or plants should be recognised as assets when:

- a) it is probable that future economic benefits associated with the asset will flow to the enterprise; and
- b) the cost or value of the asset to the enterprise can be measured reliably.

### **Measurement of Biological Assets**

**Principle 3** – Biological assets should be measured at each balance date at their fair value.

**Q 7** – *Do you agree that fair value measurement of expected future events at each balance date achieves greater relevance than historical cost?  
Are fair value measurements sufficiently reliable for financial reporting purposes?*

### **Determining Fair Value**

**Principle 4** – The primary indicator of fair value should be net market value.

**Q 8** – *Should the primary indicator of fair value be net market value?*

### **Recognition of Changes in Biological Assets**

**Principle 5** - The change in the carrying amount value for a group of biological assets should be allocated between:

- a) the change attributable to differences in fair values; and
- b) the physical change in biological assets held.

**Q 9** – *Do you believe that periodic independent external validation of the determination of fair value should be required if present value measurement methods are used by management? If so how frequently?*

**Q 10** – *Do you agree that the change in carrying amount for a group of biological assets should be allocated between:*

- a) the change attributable to differences in fair values between balance sheet dates; and
- b) the physical change in biological assets held?

**Q 11** - *If you believe that the change in carrying amount should be split (Q10), how should the components of the change in carrying amount be determined?*

**Principle 6** - The change in carrying amount attributable to the physical change in biological assets should be recognised as income or expense and identified as the change in biological assets.

**Principle 7** – The change in carrying amount attributable to differences in fair values should be recognised in the statement of non-owner movements in equity and presented in equity under the heading of surplus/deficit on fair valuation of biological assets.

**Q 12** – If you believe that the change in carrying amount should be split (Q10), where should the components be recognised (for Principles 6 and 7)

- a) both components in the income statement;
- b) the operating gain in the income statement and the holding gain in the statement on non-owner movements in equity;
- c) both components in the statement of non-owner movements in equity?

**Principle 8** – In agricultural systems in which the predominant activity has a production cycle of less than one year, for example, broiler chickens, cereal crops, nursery plants, and mushrooms, the total change in carrying amount should be reported in the income statement as a single amount of income or expense.

**Principle 9** – Extraordinary Items (as defined in IAS 8, Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies) the consequences of which will form part of the total change in biological assets should be excluded from the change in biological assets that is recognised as income or expense under Principle 6. Instead, it should be shown separately on the face of the income statement after calculation of profit or loss from ordinary activities and should also be shown as a separate item in the reconciliation required to determine the change attributable to biological transformation.

**Principle 10** – Other events that give rise to a change in biological assets of such a size, nature, or incidence that their disclosure is relevant to explain the performance of the enterprise for the period (as defined in IAS 8) should be included in the change in biological assets recognised in income and expense under Principle 6 and should also be shown as a separate item in the reconciliation required to determine the change attributable to biological transformation.

#### **Information to be Presented on the Face of the Balance Sheet**

**Principle 11** – Biological assets should be classified as a separate class of assets falling under neither current nor non-current classifications.

**Q 13** – Do you agree that biological assets should be classified as a separate class of asset?

#### **Information to be Presented either on the Face of the Balance Sheet or in the Notes**

**Principle 12** – The biological assets classification should be sub-classified according to:

- a) class of animal or plant;
- b) nature of activities – consumable or bearer; and
- c) maturity or immaturity for intended purposes.

**Principle 13** – In agricultural activities in which animals or plants themselves are to be harvested, that is, consumable, the maturity criterion will be attainment of harvestable specifications.

**Principle 14** – In agricultural activities in which the animals or plants are to bear products for harvest (that is, bearer) the maturity criterion will be the attainment of sufficient maturity to sustain economic harvests.

#### Presentation in the Income Statement

**Principle 15** – An enterprise with significant agricultural activities is encouraged to present on the face of the income statement an analysis of the income and expenses used in determining profit from operating activities using a classification based on the nature of income and expenses.

#### Disclosure

**Principle 16** – The financial statements should disclose, in respect of each subclass of biological assets:

- a) the measurement base used to derive fair value;
- b) whether an independent valuer was involved;
- c) the change in carrying amount attributable to biological transformation determined by reconciling the total change in carrying amount and disclosing the components of that change, for example:
  - i) holding gains;
  - ii) net exchange differences arising on the translation of the financial statements of a foreign entity;
  - iii) sales or disposals and purchases or additions;
  - v) extraordinary losses; and
  - vi) other movements;
- d) the existence and amounts of restrictions on title, and biological assets pledged as security for liabilities;
- e) the amount of commitments for the development or acquisition of biological assets;
- f) specific risk management strategies adopted in relation to protection of the investments in biological assets and agricultural produce; and
- g) activities that are unsustainable, with an estimated date of cessation of the activity.

**Q 14** - re Principle 16 c) Do you agree that the change in carrying amount attributable to biological transformation should be disclosed?

#### Agricultural Produce – Measurement and Presentation

**Principle 17** – Agricultural produce should be measured at each balance sheet date at fair value, to the extent that it is sourced from an enterprise's biological assets and the source biological assets are valued at fair value as proposed by this Draft Statement of Principles.

**Q 15** – Do you agree that agricultural produce should be measured at each balance sheet date at fair value?

**Principle 18** – The change in carrying amount of agricultural produce held at two balance sheet dates should be recognised in the income statement as either income or expense.

**Principle 19** – Agricultural produce harvested for trading or processing activities within integrated agricultural/agribusiness operations should be measured at the fair value at the date of harvest. This amount is the deemed cost for application of IAS 2 to consequential inventories.

**Agricultural Produce – Information to be Presented on the Face of the Balance Sheet**

**Principle 20** - Agricultural produce should be classified as inventory in the balance sheet and separately disclosed either on the face of the balance sheet or in the notes.

**Agricultural Land**

**Principle 21** – Enterprises are encouraged to utilise the allowed alternative treatment as prescribed in IAS 16 for agricultural land, particularly in land-based systems such as orchards, plantations, and forests where fair value of the biological asset has been derived from a net market value, or a surrogate measure of fair value, that is inclusive of land.

**Q 16** – In land-based agricultural systems, the SC encourages enterprises to use fair valuation of agricultural land.

*Given the relationship between agricultural land and biological assets, should this encouragement in fact be a requirement?*

**Principle 22** – Enterprises are encouraged to sub-classify land in order to disclose agricultural land in its different uses, either on the face of the balance sheet or the notes.

**Source:** Published by the IASC  
December 1996.

Originally supported by – *Agriculture* - A Note from the Staff  
Agenda Paper 15, IASC Board Meeting, Barcelona, September 1996.



## Appendix 11: IASC – Respondents to DSOP ‘Agriculture’

### Member Bodies and Other Accounting Bodies

#01	Fédération des Experts Compatibles Européens	[FEE]
#02	Federación Argentina de Consejos Profesionales de Ciencias Económicas	
#03	Australian Society of Certified Practising Accountants	[ASCPA]
#04a	Institute of Chartered Accountants in Australia	[ICAA]
#04b	Institute of Chartered Accountants in Australia [additional comments]	
#05	Canadian Institute of Chartered Accountants (staff)	[CICA]
#06	Certified General Accountants’ Association of Canada	[CGA]
#07	Society of Management Accountants of Canada	[CMA]
#08	Institute of Chartered Accountants of England and Wales (Draft with #31)	[ICAEW]
#09	Institut der Wirtschaftsprüfer [Germany]	[IDW]
#10	Malaysian Institute of Accountants	[MIA]
#11	Institute of Chartered Accountants of New Zealand	[ICANZ]
#12	Stowarzyszenie Księgowych W Polsce (Accountants Assn. of Poland)	
#13	Câmara dos Revisores Oficiais de Contas [Portugal]	
#14	South African Institute of Chartered Accountants	[SAICA]
#15	Föreningen Auktoriserade Revisorer [Sweden]	[FAR]
#16	Institute of Chartered Accountants of Zimbabwe	[ZICA]

### Standard Setting Bodies

#17	European Commission	[EU]
#18	Australian Accounting Research Foundation	[AARF]
#19	Raad voor Jaarverslaggeving [Council, of Annual Reporting] [Netherlands]	[CAR]

### Financial Analyst Group

#20	Association for Investment Management and Research	[U.S.A.]
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### Financial Regulator Sector

#21	Danish Financial Supervisory Authority	[Denmark]
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### Accounting Firms/Accountants

#22	Arthur Anderson LLP [International]	
#23	Coopers & Lybrand [International]	
#24	Deloitte Touche Tohmatsu International	
#25	Martin O’Connor, FCA	[Australia]
#26	Edgar Albrow, FCA	[UK]

### Industry Representative Groups

#27	Group of 100 Inc.	[Australia]
#28	Swedish and Finnish Forest Based Companies	
#29	British Bankers Association	[U.K.]

### Banks and Financial Institutions

#30	World Bank	
#31	Barclays Bank (UK - Includes draft of #08)	

<b><u>Industry &amp; Commerce – Individual Companies</u></b>		-	<b><u>SGARA type</u></b>	
#32	Broken Hill Proprietary Limited			[Australia]
#33	North Limited		<i>Forestry</i>	[Australia]
#34	Landcorp Farming Limited		<i>Livestock</i>	[New Zealand]
#35	Sappi		<i>Forestry</i>	[South Africa]
#36	Dalgety Limited	<i>Pig and Poultry breeding + Salmon farming</i>		[U.K.]
<b><u>Public Sector</u></b>				
#37	International Federation of Accountants	[IFAC - Public Sector Committee]		
#38	Farm Financial Standards Council		[FFSC]	[USA]
<b><u>Academics</u></b>				
#39	Don Roberts - for Austin Adams, University of New England			[Australia]
#40	Professor Ron Peterson and Kathy Herbohn, James Cook University			[Australia]
#41	Colin Saunderson, University of Cambridge			[U.K.]
<b><u>Other</u></b>				
#42	Australasian Council of Auditors-General		[ACAG]	[Australia]

**Source:** List extracted from Comment Letters received to Draft Statement of Principles – ‘Agriculture’

Published by the IASC  
8 August 1997

**Appendix 12: Abstract to the Australian Government Rural Industries Research  
and Development Corporation - Research Project No. AAR-A1**

**‘Development of an accounting standard for  
self-generating and regenerating assets’**

**Researcher: Robert Keys at the Australian Accounting Research Foundation.**

**Objectives**

To develop accounting standards on self-generating and regenerating assets (SGARAs) that prescribe the recognition, measurement and disclosure rules to be followed in reporting SGARAs and the related revenue in the financial reports of both public and private sector entities.

**Background**

Prior to this project being undertaken, there were no accounting standards that dealt specifically with SGARAs. Preliminary research identified how important SGARA related industries are to the Australian economy, and the diverse financial reporting practices that have emerged within those industries. The lack of accounting standards for SGARAs was seen by many as leading to non-comparable reporting resulting in a barrier to investment in SGARA related industries.

**Research**

SGARAs are defined as non-human living assets and include livestock (including sheep and cattle); trees in pine plantations, native forests and orchards; vines in vineyards; and other biological assets held for commercial purposes. They are unique in that they change in biological form over their lives. Traditional historical cost accounting was seen as inadequate in dealing with the uniqueness of SGARAs because the value of biological change that occurs naturally as a result of cost-less inputs (for example rainfall or sunlight) is not adequately reflected in the costs incurred in managing SGARAs. In addressing this, the project concluded that SGARAs should be measured at current values (in particular net market values). The Standards that resulted from the project provide guidance on the determination of net market value whether or not an active and liquid market for the SGARAs exists.

Measuring SGARAs at net market value gives rise to the question of how to account for the change in net market value that may occur during a reporting period. The project considered various alternatives, including:

- recognising the entire change directly in equity
- recognising the change attributable to biological change in the profit and loss statement and recognising the change attributable to price change directly in equity and
- recognising the entire change in the profit and loss statement

### **Outcomes**

The project resulted in the issue of Australian Accounting Standard AAS 35 and Accounting Standard AASB 1037 "Self Generating and Regenerating Assets", applicable to reporting periods ending on or after 30 June 2000

### **Implications**

The project concluded in favour of recognising the entire change in the profit and loss statement on the basis that it provides more relevant information on the financial performance of the SGARAs.

Another consequence of measuring SGARAs at net market value is the question of how to account for the non-living produce of SGARAs. Because non-living produce is not a SGARA, it would fall within the scope of existing Standards (particularly those that relate to accounting for inventories) and would be required to be measured at the lower of cost and net realisable value. The project concluded that it would be unreasonable to require SGARAs to be measured at net market value and then to require the non-living produce extracted therefrom to be measured at cost. To address this issue, the project concluded that the net market value of non-living produce immediately after it becomes non-living should be deemed to be the cost of the non-living produce.

The Standards also prescribe presentation of and disclosures about SGARAs that provide users of financial reports with relevant and reliable information to enable them to make resource management allocations.

Issued during 1998 by Robert Keys, on behalf of the AARF.

**Source:** RIRDC Sub-Program 4.2 - Resilient Agricultural Systems Completed Projects in 1998-1999

Note

The RIRDC did not identify the Report date within its List of Completed Projects for 1998-99.

This Report was probably issued during third quarter, 1998, prior to the issue of the AAS 35/AASB 1037 standards.

**Appendix 13: AARF – Respondents to ED 83**  
**‘Self-Generating and Regenerating Assets’**  
**(# - In Received Submission Order)**

**Auditor General**

#32	Australasian Council of Auditors-General	[ACAG]	ACT
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**Public Sector**

#41	Dept. of Treasury and Finance Tasmania		Tasmania
#17	New South Wales Treasury		NSW
#24	Queensland Treasury		Queensland
#03	Treasury West Australia		West Australia

**Member Bodies and Other Accounting Bodies**

#44	Australian Society of Certified Public Accountants	[ASCPA]	Melbourne
#16	The Institute of Chartered Accountants in Australia	[ICCA]	Sydney

**Accounting Firms/Accountants**

#09	Arthur Andersen		Melbourne
#45	Coopers & Lybrand	[Mark Johnson]	Sydney
#40	Deloitte Touche Tohmatsu	[Bruce Porter]	Melbourne
#39	Ernst & Young		Melbourne
#37	KPMG	[Michael West]	Melbourne
#35	Price Waterhouse	[David Brown]	Sydney
#27	Graham Lindsay, Lindsay Associates Pty Limited	CA	Victoria
#33	Pitcher Partners	[Don Rankin] CA	Melbourne
#30	Robert B. Walker	CA	N.Z.

**Industry Representative Groups – SGARA Entities**

#20	Group of 100 Inc.		Melbourne
#36	Winemakers’ Federation of Australia Inc.	[Stephen Strachan]	South Australia

**Industry & Commerce – Agricultural Entities – Non-Bearer SGARAs – Private Sector**

#14	Amcor Limited	<i>Forestry</i>	Victoria
#04	Auscott Limited	<i>Crop (Cotton)</i>	NSW
#31	Colly Cotton Group of Companies	<i>Crop</i>	Victoria
#25	East African Coffee Plantations Limited	<i>Orchards</i>	South Australia
#11	Futuris Corporation Limited	<i>Livestock</i>	West Australia
#26	Landcorp Farming Limited	<i>Livestock</i>	N.Z.
#12	North Forest Products Limited	<i>Forestry</i>	Tasmania

**Industry & Commerce – Agricultural Entities – Non-Bearer SGARAs – Public Sector**

#29	ACT Forests (Dept. of Urban Services)	<i>Forestry</i>	ACT
#10	Dept. of Conservation and Land Management	<i>Forestry</i>	West Australia
#21	Dept. of Primary Industries	<i>Forestry</i>	Queensland
#42	Dept. for Administrative and Information Services	<i>Forestry</i>	South Australia
#19	Forestry Tasmania	<i>Forestry</i>	Tasmania
#28	Natural Resources and Environment	<i>Forestry</i>	Victoria
#15	State Forests of New South Wales	<i>Forestry</i>	NSW
#34	Victorian Plantations Corporation	<i>Forestry</i>	Victoria

**Industry & Commerce – Agricultural Entities – Bearer SGARAs**

#13	BRL Hardy Limited	<i>Vines</i>	South Australia
#05	Cape Mentelle Vineyards Limited	<i>Vines</i>	West Australia
#22	Foster's Brewing Group Limited	<i>Vines</i>	Victoria
#08	Peter Lehmann Wines	<i>Vines</i>	South Australia
#18	Southcorp Limited	<i>Vines</i>	South Australia

**Industry & Commerce – Non-Agricultural Entities**

#02	The Broken Hill Propriety Company Limited		Melbourne
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**Academics**

#07	Andrew (A.N.) Priest	Edith Cowan University	Perth
#06	Don (D.L.) Roberts	The University of New England	Armidale
#46	Don (D.L.) Roberts	The University of New England	Armidale
#23	John (J.B.) Ryan	University of Western Sydney	Macarthur

**Financial Analyst Group**

#38	Securities Institute of Australia (Craig Drummond)	[ASIA]	Sydney
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**Valuers**

#43	Australian Institute of Valuers and Land Economists (Inc.)	[AIVLE]	ACT
#01	J.I. Cone		Victoria

**Source:** Australian Accounting Research Foundation:

List of Respondents Cover Sheet to Submissions on ED 83: 'Self-Generating and Regenerating Assets'

## Appendix 14: IASC – Respondents to E65 ‘Agriculture’

### Standard Setting Bodies

Australian Accounting Research Foundation	[AARF]	[Australia]
Danish Accounting Standards Committee	[DASB]	[Denmark]
European Commission	[EU]	[Europe]
Instituto Mexicano de Contadores Públicos	[IMCP]	[Mexico]
Lembaga Piawaiian Parakaunan Malaysia/Malaysian Accounting Standards Board	[MASB]	[Malaysia]
Raad voor de Jaarverslaggeving - Council for Annual Reporting	[CAR]	[Netherlands]

### Other

Australasian Council of Auditors-General	[ACAG]	[Australia]
Instituto de Auditores-Censores Jurados de Cuentas de España		[Spain]

### Member Bodies and Other Accounting Bodies

American Institute of Certified Public Accountants	[AICPA-AcSEC]	[U.S.A.]
Chartered Institute of Management Accountants	[CIMA]	[U.K.]
Conseil National de la Compagnie nationale des commissaires aux comptes		[France]
Federación Argentina de Consejos Profesionales de Ciencias Económicas		[Argentine]
Fiji Institute of Accountants [via Prof M White, University of South Pacific]		[Fiji]
Föreningen Auktoriserade Revisorer [The Swedish Institute of Authorised Public Accountants]	[FAR]	[Sweden]
Institut der Wirtschaftsprüfer	[IDW]	[Germany]
Institute of Certified Public Accountants in Bulgaria		[Bulgaria]
Institute of Certified Public Accountants of Kenya	[ICPK]	[Kenya]
Institute of Cost and Management Accountants of Pakistan	[ICMA]	[Pakistan]
Institute of Management Accountants	[IMA]	[U.S.A.]
Joint International Committee of CNDC and CNR		[Italy]
Malaysian Institute of Accountants/Institut Akauntan Malaysia	[MIA]	[Malaysia]
Ordem dos Revisores Oficiais de Contas		[Portugal]
The Association of Chartered Certified Accountants	[ACCA]	[UK]
The Canadian Institute of Chartered Accountants	[CICA]	[Canada]
The Institute of Chartered Accountants	[ZICA]	[Zimbabwe]
The Institute of Chartered Accountants in Australia	[ICAA]	[Australia]
The Institute of Chartered Accountants in England & Wales	[ICAEW]	[U.K.]
The Japanese Institute of Certified Public Accountants	[JICPA]	[Japan]
The Korean Institute of Certified Public Accountants	[KICPA]	[Korea]
The National Board of Accountants and Auditors	[NBAA]	[Tanzania]
The South African Institute of Chartered Accountants	[SAICA]	[South Africa]
Truehand Kammer [Institute of Certified Accountants and Tax Consultants]		[Switzerland]

### Accounting Firms/Accountant Groups

Arthur Andersen International		[U.S.A.]
Deloitte Touche Tohmatsu		[New York]
Ernst & Young International		[London]
PricewaterhouseCoopers		[London]
International Association of Financial Executives Institutes	[IAFEI]	[London]
International Federation of Accountants - Public Sector Committee	[IFAC]	[U.S.A.]

**Public Sector****Industry Representative Groups**

Canadian Farm Business Management Council	[CFMBC]	[Canada]
Coillte Teoranta / The Irish Forestry Board Limited		[Ireland]
Industrie-Holding	[Federation of Swiss Industrial Holding Companies]	[Switzerland]
Group of 100 Inc.	[G100]	[Australia]

**Industry & Commerce – Agricultural Entities -****SGARA types**

East African Coffee Plantations Limited	<i>Orchardist</i>	[Australia]
Eastern Produce Kenya Limited	<i>Tea</i>	[Kenya]
Illovo Sugar Limited	<i>Sugar</i>	[South Africa]
North Group Limited	<i>Forestry</i>	[Australia]
Nutreco International B.V.	<i>Pig/Poultry breeding &amp; Salmon farming</i>	[Netherlands]
Southcorp Holdings Limited	<i>Wine</i>	[Australia]

**Industry & Commerce – Non-Agricultural Entities**

Ascom Management AG		[Switzerland]
F. Hoffman-La Roche Ltd.		[Switzerland]
Nestlé S.A.		[Switzerland]
Sulzer Management Limited		[Switzerland]

**Academics**

Don [D.L.] Roberts,	University of New England, Armidale	[Australia]
Dr Matthais Amen	University of Berne	[Switzerland]
Prof Asish Bhattacharyya	Calcutta University	[India]
Prof Hajime Arai	Tokyo University of Agriculture	[Japan]
Prof. Royji Abe	Kyoto University	[Japan]

**Financial Analyst Groups**

Association for Investment Management and Research	[AIMR]	[U.S.A.]
International Actuarial Association		[Canada]
The Security Analysts Association of Japan	[SAAJ]	[Japan]

**Source:** Extracted from Submissions on E65 'Agriculture'  
to the International Accounting Standards Committee.



**Appendix 15: IASC FIELD TEST PROJECT - AGRICULTURE****REPORT on FIELD TEST FINDINGS**

NOT FOR RELEASE TO THE  
PUBLIC OR THE PRESS

IASC BOARD MEETING  
COPENHAGEN, JUNE 2000  
AGENDA PAPER 7G

**Agriculture**  
*Report on Field Test Findings*

**Introduction**

1. This Agenda Paper briefly outlines the procedures followed in conducting the field test and then summarises the results obtained up to 31 May. Agenda Paper 7H is a spreadsheet analysis of the responses.
2. At its meeting in March 2000, the Board asked the IASC Staff to complete a field test of the practicability of fair value measurements before the Board's meeting in June 2000.

**Field Test Approach**

3. In April 2000, the IASC Staff sent letters requesting participation in the field test along with the field test questionnaire to 78 agricultural companies, four (4) consultants or accounting firms, one (1) business representative group, and one (1) institute of accountants. These companies or organisations included companies that expressed interest to the IASC Staff, E65 respondents, companies suggested by the IASC Board members, Agriculture Steering Committee members and the IASC Staff. The IASC Staff also identified some companies from public companies' database. The questionnaire was posted to the IASC public website. 18 replies  
} 84
4. It was stated in the questionnaire that the Staff would not associate an individual company with a particular response, while a summary of responses would be presented to the IASC Board and the Steering Committee. The questionnaire was accompanied by a copy of the E65. A copy of the field test questionnaire is provided as Appendix 2 to this Agenda Paper.
5. Each participant was asked to determine fair value for its most significant biological asset and for its most significant item of agricultural produce. Respondents generally had one principal biological asset. Respondents generally did not have any significant agricultural produce because either the biological asset is sold directly or the time between harvest and sale of the produce is very short, resulting in insignificant produce inventory.

**Summary of responses****General Information of Participants (Part A: 5, 11, 14)**

6. 18 responses were received, including ten (10) listed companies and five (8) non-listed companies.
7. The following table summarises the countries where the participants are based:

Area	No.	Countries <i>Sugar &amp; Forestry</i>	<i>Tea</i>
Africa	3	2 from South Africa, 1 from Kenya	
Asia	2	1 from Japan, 1 from Sri Lanka <i>B</i>	<i>Tea</i>
Oceania	9	6 from Australia, 2 from New Zealand, 1 from Papua New Guinea <i>Livestock &amp; Forestry</i>	<i>Sugar 17</i>
Europe	2	2 from Netherlands <i>Livestock &amp; Potatoes</i>	<i>18</i>
North America	1	1 from US <i>Forestry</i>	
South America	1	1 from Guyana <i>Sugar 16</i>	
	18		

8. The following table summarises industries represented by the participants, together with countries:

Industry	No.	Countries <i>13</i>
Forestry	6	2 from Australia, 1 from Japan, 1 from New Zealand, 1 from South Africa, 1 from US
Livestock	4	2 from Australia, 1 from Netherlands, 1 from New Zealand, <i>Ab 23</i> <i>Solomon H</i> <i>6</i>
Sugar	3	1 from Guyana, 1 from Papua New Guinea, 1 from South Africa <i>16</i> <i>17</i> <i>12</i>
Tea	2	1 from Kenya, 1 from Sri Lanka* <i>5</i>
Wine/Grapes	2	2 from Australia <i>4 = S' Corp</i> <i>9 =</i>
Potatoes	1	1 from Netherlands <i>18</i>
	18	

\* The Sri Lankan company is involved in tea and rubber.

**Biological Assets - Basis of determining fair value (Part B: 4)**

9. The field test questionnaire asked participants to state which basis was used for determining fair value. Paragraphs 24-26 of E65 provide 8 bases.
10. The following table summarises the bases used by the participants:

	<i>Basis</i>	<i>No.</i>	<i>Industry</i>
a.	Market price in its location (para 24 of E65)	4	2 from livestock, 2 from sugar
b.	Market price in another location (para 25 of E65)	1	1 from livestock
c.	Market price based on known transactions (para 26(a) of E65)	1	1 from wine/grapes
d.	Market price for similar / related assets (para 26(b) of E65)	0	
e.	Sector benchmark (para 26 (c) of E65)	0	
f.	Net present value (para 26(d) of E65)	6	5 from forestry, 1 from wine/grapes
g.	Net realisable value (para 26(e) of E65)		
h.	Cost (para 26(f) of E65)		
i.	Other basis	1	1 from sugar
j.	Impossible to estimate fair value reliably	4	1 from forestry, 1 from livestock, 1 from tea, 1 from tea/rubber
	Total	17*	

\* One company did not answer for its biological asset (while it answered for its agricultural produce).

**Biological Assets - Subjective reliability (Part B: 7, 3d.)**

11. The field test questionnaire asked participants to indicate their subjective assessment or reliability of their fair values.
12. The following table summarises the participants' assessment.

	<i>No.</i>	<i>Industry</i>	<i>Basis</i>
Highly reliable	1	1 from livestock	1 used market price in its location
Reliable	7	2 from forestry, 2 from livestock, 2 from sugar, 1 from wine/grape	3 used market price in its location 2 used net present value 1 used market price in another location 1 used market price based on known transactions
Not reliable	6	2 from forestry, 1 from livestock, 1 from tea, 1 from tea/rubber, 1 from wine/grape	3 used net present value 3 stated it was impossible to value reliably
No position	3	2 from forestry*1, 1 from sugar	1 used net present value*1 1 used a basis that is not stated in E65 1 stated it was impossible to value reliably
Total	17*2		

\*1 One forestry company (that used net present value) stated that its fair value is reliable and there were no problems in making the valuation because it used a recently acquired tract of land with recently inventoried timber. The company stated that the asset cannot be valued reliably on a consistent basis at regular reporting dates. (Company No. 14)

\*2 One company did not answer for its biological asset (while it answered for its agricultural produce).

13. The field test questionnaire also asked participants whether they believe that the asset can be valued reliably on a consistent basis at regular reporting dates using the same technique used in their fair value measurements.
14. The following table summarises the participants' views.

	<i>No.</i>	<i>Industry</i>	<i>Basis</i>
Yes, can be valued reliably on a consistent basis	9	3 from livestock, 3 from sugar, 2 from forestry, 1 from wine/grape	4 used market price in its location  2 used net present value  1 used market price in another location  1 used market price based on known transactions  1 used a basis that is not stated in E65
No	5	2 from forestry, 1 from livestock, 1 from tea/rubber, 1 from wine/grape	3 used net present value  2 stated it was impossible to value reliably
No position	3	2 from forestry, 1 from tea	1 from Australia, 1 from Kenya, 1 from Japan
Total	17*		

\* One company did not answer for its biological asset (while it answered for its agricultural produce).

15. Detailed reasons for the participants' assessment are included in Appendix 1 to this Agenda Paper. Some of those who answered "not reliable" expressed concerns about subjectivity of fair value measurements arising from assumptions when there is no active market.

**Biological assets - Problems that arose in making the valuation (Part B: 5)**Forestry

16. The following difficulties were indicated by forestry participants (who used net present value as a basis):
  - (a) to determine different ratings of growing forests
  - (b) to estimate future prices and costs
  - (c) to determine discount rate
17. Some forestry participants indicated that they would incur significant costs for physically investigating forests, modelling the net present value exercise, etc.

Livestock

18. One participant indicated that the costs were incurred in enhancing the cattle management. It made a reliable estimate of weights of cattle based on the age of the herd, since it is impractical to weigh each beast regularly (360,000 head of cattle are in a number of locations.) Market prices are determined based on weight per head of cattle.
19. One participant indicated it is difficult to determine a fair value for the different weights of salmon when market prices depend also on quality, which is not known until harvest.
20. 2 participants indicated that there were no problems.

Tea/rubber

21. 2 participants indicated that net cash flow projections are not reliable due to the long period (20 year, 50 year), too many subjective assumptions such as weather.

Sugar

22. 2 participants stated that the only problem relates to the valuation of partly grown cane. They also stated that a linear representation of biological growth curve was used.
23. Detailed comments are included in Appendix 1 to this Agenda Paper.

**Agricultural Produce**

24. 3 participants filled in Part B for their agricultural produce (grapes, wool, and potatoes). 3 forestry companies indicated that Part B is not applicable for their agricultural produce since (i) no significant inventories are maintained (company No. 2 and No. 13) or (ii) since the nature of the produce is substantially the same as biological assets (company No. 7).

**Agricultural Produce - Basis of determining fair value (Part B: 4)**

25. 2 participants (Australia and New Zealand) used the market price in its location for determining fair value of their agricultural produce (grapes and wool). (Company No. 4 and No. 6)
26. One participant (Netherlands) used 3 bases for determining fair value of their potatoes (Company No. 18):
- (a) For the Bintje variety, where weekly market prices are available, market price for an identical asset was used.
  - (b) If a variety was at stake other than Bintje, the price is related to Bintje with a deduction or add up of the normal price difference (from previous years in no additional information is available) between Bintje and the variety at stake.
  - (c) We also used net realisable value, based on a contract price already agreed upon with a willing buyer. Or in the case where the contract price is partly tied to the market price at the moment of delivery (e.g. Euro 10 pr 100 kg with 25% of the difference between Euro 10 and the actual market prices added), we used the market price as in b and d above as the benchmark. Future contracts are not taken into account, but valued as a financial asset at fair value separately.

**Agricultural Produce - Subjective reliability (Part B: 7, 3d.)**

27. One participant stated that its fair value (of wool) is highly reliable.
- (a) Based on current actual sales evidence for "identical" assets. (company No. 6) *wool sale*
28. One participant stated that its fair value (of potatoes) is reliable.
- (a) The estimation of the volume in stock is difficult. We feel that the valuation is more reliable than an estimation of historical cost, as this needs highly debatable assumptions on the allocation of joint costs (labour, depreciation of tractors etc.) to the different products. Contract farming can make the use of market quotation and sector benchmarks more difficult. (company No. 18)
29. One participant stated that its fair value (of grapes) is reliable, while it stated that the asset cannot be valued reliably on a consistent basis. (company No. 4)

- (a) On a scale of 1-10, rate the reliability and representation of the Utilisation Surveys as an 8. There is a high degree of involvement of major buyers who account for >80% of the annual intake of wine grapes.
- (b) Cannot value reliably consistently: We believe grapes can be reasonably valued at the time of harvest or when they are picked. This would be an estimate at best because the final grape classification for the end product, is not finalised until July/early August, which is insufficient time for inclusion in the year end statutory accounts.
- (c) Further, while prices can be estimated, the regional price survey is not published until the end of August, which is too late for inclusion in the annual statutory accounts.

**Agricultural Produce - Problems that arose in making the valuation (Part B: 5)**

- 30. 3 participants indicated that there were no significant problems.
  - (a) No major problems. The estimation of the volume of the potatoes in storage is probably more difficult (unless you make the accounts many months later, after the actual sale and delivery in the next accounting year. (company No. 18)



**Fair value used in making business management decisions (Part B: 8)**

31. The field test questionnaire asked participants whether they use information about fair value in making business management decisions.
32. The following table summarises the participants' answers:

	<i>No.</i>	<i>Industry</i>	<i>Country</i>
Yes	12*	6 from forestry, 3 from livestock, 1 from sugar, 1 from wine/grapes, 1 from potatoes	5 from Australia, 2 from New Zealand, 2 from South Africa, 1 from Japan, 1 from Netherlands, 1 from US
No	5	2 from sugar, 1 from livestock, 1 from tea/rubber, 1 from wine/grapes	1 from Australia, 1 from Guyana, 1 from Netherlands, 1 from Sri Lanka, 1 from Papua New Guinea
No comment	1	1 from tea	1 from Kenya
Total	18		

\* One company (Netherlands) stated that it uses fair value of its agricultural produce (potatoes) and did not comment on their biological asset. One company (New Zealand) stated that it uses fair value of its biological asset and agricultural produce (wool).

33. Detailed comments are included in Appendix 1 to this Agenda Paper.

**Reporting in the balance sheet (Part B: 9)**

34. The field test questionnaire asked participants whether their biological assets or agricultural produce are reported at cost or fair value, currently.
35. The following table summarises the participants' answers for biological assets:

	<i>No.</i>	<i>Industry</i>	<i>Country</i>
Cost	7	3 from forestry, 2 from livestock, 1 from sugar, 1 from tea/rubber	1 from Australia, 1 from Japan, 1 from Netherlands, 1 from New Zealand, 1 from Sri Lanka, 1 from South Africa, 1 from US
Fair value	7	3 from forestry, 2 from livestock, 1 from tea, 1 from wine/grapes	4 from Australia, 1 from Kenya, 1 from New Zealand, 1 from South Africa
Other basis	1	1 from wine/grapes	1 from Australia
Not reported in B/S	1	1 from sugar	1 from Guyana
No comment	1	1 from sugar	1 from Papua New Guinea
Total	17*		

\* One company did not answer for its biological asset (while it answered for its agricultural produce).

36. Regarding agricultural produce, 2 participants (from Netherlands and New Zealand) stated that their agricultural produce (potatoes and wool) is reported at fair value. One participant (Australia) stated that its agricultural produce (grapes) is reported at cost.
37. Detailed comments are included in Appendix 1 to this Agenda Paper.

**Implications for the Standard**

- 38. 6 participants (5 forestry and one wine/grapes) used net present value as a basis of fair value measurements. In addition, two (2) participants (tea and tea/rubber) indicated that it is impossible to value their assets reliably since the net present value would not be reliable (as they would use net present value as a basis). As there is no hierarchy in paragraph 26 of E65, there is a possibility that enterprises would use net present value while market-based measures (e.g. market prices for similar assets) are available. The Steering Committee agreed that in many cases, measures of fair value based on market prices will result in greater reliability and comparability than would measures of fair value derived from individual company-specific present value calculations. The Steering Committee has modified the draft Standard to clarify this matter.
- 39. It appears that the problems arise, in particular, in measuring the fair value of biological assets when there is no active market and the net present value basis is used. That is, too many assumptions (e.g. weather) are involved and then the fair value becomes subjective. Some participants expressed concerns about comparability from a user perspective (e.g. due to different approaches to the same issue such as discount rate). The Steering Committee added guidance on how net present value calculations should be done.
- 40. Some participants indicated that significant costs would be incurred for physically investigating forests, modelling the net present value exercise, etc. The Steering Committee did not make any changes specifically in response to the cost question. 12 participants (of 18) indicated that they do measure and use fair values already in making business management decisions.
- 41. Because of concerns expressed by field test participants, the Board might consider having a "reliability exception." That is, the final Standard might state that a biological asset should be measured at cost in cases in which an enterprise will not be able to determine the fair value of the asset reliably on a continuing basis. It might state a presumption that fair value can be reliably measured but that the presumption can be overcome if there are no market-based prices and no other means to calculate fair value (such as net present value). The Steering Committee does not support a reliability exception. It believes that fair value and changes in fair value are far more relevant than cost as an indicator of performance, that fair values are already measured and used internally by many agricultural enterprises, and that because of the substantial allocations involved, cost often is no more reliably measurable than fair value.

asset  
or the  
produce

but 8 v 6 reliable v non reliable of fair values  
 9 v 5 asset valued reliably on a continuing basis      pages of problem  
 12 v 5 FV for management decisions  
 7 v 7 FV for assets  
 FV Cost  
 FV 2 v 1 FV for produce  
 produce Cost grapes

10 v 7 assets & produce for investors / creditors  
 Net Favour

**Comment on E65 in General (Part B: 10)**

42. The field test questionnaire asked participants whether they favour the proposal in E65 that, for financial reporting to investors and creditors, all biological assets be measured at fair value and that, at the point of harvest, all agricultural produce be measured at its fair value.
43. The following table summarises the participants' views:

	No.	Industries	Countries
Do not favour	10	4 from forestry, 2 from livestock, 2 from wine/grapes, 1 from sugar, 1 from tea	4 from Australia, 1 from Japan, 1 from Kenya, 1 from Netherlands, 1 from New Zealand, 1 from South Africa, 1 from US
Favour	7	2 from forestry, 2 from livestock, 2 from sugar, 1 from potatoes	2 from Australia, 1 from Guyana, 1 from New Zealand, 1 from Netherlands, 1 from Papua New Guinea, 1 from South Africa
No explicit position	1	1 from tea/rubber	1 from Sri Lanka
	18		

44. The detailed comments are included in Appendix 1 to this Agenda Paper. Some participants who did not favour indicated that fair value changes should not be recognised in the net profit and loss. Some participants expressed concerns about subjectivity / reliability of fair value measurements.

**Appendix 1**  
**Detailed comments in the responses to the field test questionnaire**

**1. Biological assets - Reasons for reliability assessment (Part B: 7)**

Highly reliable

- livestock

- (a) Based on current actual sales evidence for "identical" assets. (company No. 6)

Reliable

- livestock

- (a) Market prices are driven by market factors, including (1) economic conditions of the market, (2) quality of the product, (3) Socio-political influences, and (4) consumer taste. (company No. 1)

- forestry

- (a) The valuation is based on current and/or best data available in the business and the NPV method best parallels the way our business processes work. Reliability is all relative to choices of discount rate, estimation of forest growth etc. (company No. 2)
- (b) The main problem area is the determination of the selling price, as often a free market does not exist for the various products produced by the plantations. We are currently investigating ways of linking the selling price to the world market price of the final product. This will be done by assessing the value chain from the standing tree to the finished product. (company No. 10)

- wine/grape

- (a) Prior to the adoption of the Australian accounting standard AASB 1037 "Self Generating and Regenerating Assets", the Group accounting policy on the valuation of non-current assets was to measure grape vines (recognised as part of property, plant and equipment) at Directors' Valuation. This amount was established from estimates made by independent valuers. We therefore had previous experience with valuers who were experienced in valuing our vineyards. The booked asset valuation was also subject to third party confirmation from our independent auditors. (company No. 9)
- (b) The grape harvesting period in Australia is predominantly March - May. At the end of this period, valuation for grapes from each growing region is identifiable on a market basis. This market value result for grapes is directly related to the value of grape vines. (company No. 9)

- sugar

- (a) The market price of the end product, which is raw sugar, is known. From this, it is possible to impute a value to the input material which is sugar cane. We are also able to compare fair value with our own internal cost records. (company No. 16 and 17)

Not reliable

## - forestry

- (a) The information may prove to be unreliable, though the degree of unreliability (and hence its acceptableness for financial reporting purposes) is impossible to tell at this stage. (company No. 7)
- (b) Subjectivity associated with assumptions made in determining NPV. (company No. 12)

## - wine/grape

- (a) Disagree with a separate fair value for vines as it is subjective and extremely variable, given there is no active market in vines. (company No. 4)
- (b) Due to estimates and subjectivity, valuation of the vines is open to substantial variability and/or manipulation. (company No. 4)
- (c) Determining the fair value of a vineyard involves estimating the yield in tonnes, applying estimated grapes prices and costs for a number of years into the future, together with estimating a terminal or perpetuity value and then applying an appropriate discount rate to calculate the net present value. The value of the vine is then determined as a residual in the valuation process because it is calculated by deducting the current unimproved value of land, trellis, irrigation, water licence at each reporting date from the aggregate fair value. (company No. 4)

## - livestock

- (a) Any attempt to give a fair market value of total inventory given the size distribution of fish in inventory will be arbitrary and very subjective. (company No. 11)

## -tea/rubber

- (a) There is no practical market for tea bushes. Costs can be determined reliably from normal historic methods. The biological assets in our case, tea bushes, have a life of over 50 years and, the vagaries of weather can have both significant positive and negative effects on cash flow projections and, therefore, NPV of expected cash flows cannot be reliable - too many subjective assumptions!! (company No. 5)

Cannot value reliably on a consistent basis

## - Livestock

- (a) Cannot value salmon reliably consistently since: (Company No. 11):
  - a. In the salmon farming business there is no market for salmons with a weight below 2 kg (worthless in the market). Fair value is 0? In general the salmon farming market is insufficiently transparent and mature for a fair value model to work satisfactorily.
  - b. For salmons of 2 kg there is maybe a market but we will never be able to sell it's total stock of salmons of 2 kg for the "existing market price" because the volume would have a significant impact on the price. How to determine fair value?

- c. World-wide administrative procedures and controls should be implemented which gives a true and fair view on central level on each measurement date on the balance of live-stock, given the fact that the fair value principles should be applied. Our fear is that fair value measures will add considerable administrative costs and procedure measures that are less reliable than measures of costs.

- Forestry

- (a) Cannot value reliably consistently: The methods we have used over the last 10 years to value forests (for a period these were put on B/S), was NPV and its components can be subjective and small changes to the assumptions can have a dramatic effect on the valuations. (Company No. 12)

Reliable, but the asset cannot be valued reliably on a consistent basis (Company No. 14)

- Forestry

- (a) There were no problems in making the valuation because we used a recently acquired tract of land with recently inventoried timber.
- (b) Reliable in the context of evaluating a single acquisition at a single point in time. During the acquisition process, generally more information is available to strengthen assumptions. This information is provided by the seller as part of the sales process and the buyer as part of the analysis and due diligence process. In the ongoing course of business, this information is not always readily or inexpensively available to provide as reliable a valuation for all of the timber throughout the company.
- (c) Since timber is a long term asset, many assumptions are made regarding future product prices, growth rates, and inventory levels. These assumptions are used to prepare a harvest plan that generates the revenue and cost estimates for the valuation model. Depending on a forester's estimate of volumes or the source for future prices, current valuations could potentially have significant variations.

**2. Biological assets - Problems that arose in making the valuation of biological assets (Part B: 5)**

Forestry

- (a) The extent of costs revolves around administrative activities for inventory modelling, wood yield predictions, revenue and cost data extraction, manipulation and input. Estimate of time involves approx. 3 weeks or \$5,000. (company No. 2)
- (b) Modelling the NPV was a difficult process that involves a number of estimates. More problematic aspects included, (1) determining different "ratings" for different areas under forest, (2) estimating future prices and costs, and (3) determining the discount rate. (company No. 7)
- a. Re (1), need to determine "ratings" so that each forest coupe could be classified appropriately and its future growth modelled. Factors such as soil, sunlight and altitude impact on the growth potential rating of each coupe. In their case, the best land area can grow trees to maturity in 12 years, and the worst in 30 years. This task is complicated by a lack of appropriate historical data. (Difficult to physically verify the model as physical stock takes are not taken until year 7 and then only every 3 or more years.)
- b. Re (2), estimating prices up to 30 years in advance is highly judgemental because of the long-term nature of the business.
- c. Re (3), there was some contention about whether rates should differ where land is owned as against rented, and whether the rate used should be for separate parcels of forest or the entire holding/portfolio (risk, and hence the discount rate, would be higher if an area by area approach was adopted). (Refer to Group of 100 comment letter on E65)
- (c) Will incur perhaps approx. AUD 500,000 plus system costs in the initial year. This is high proportionally when compared to the asset value. (company No. 7)
- (d) Arriving at the discount rate of 10 %. This needs to be reviewed on a regular basis to the actual returns being made. (company No. 10)
- (e) Accuracy of the spatial data is a key driver in long-term rotation crops because of nature's effect on the biological asset. (company No. 10)
- (f) Being 1 of only 2 significant forestry companies in NZ (with approx 25% of NZ estate), there is insufficient reliable market data on the few transactions there are hence use of NPV. However the experience with using NPV, it can easily lead to manipulation of the value which can be easily done with small changes to assumptions used especially discount rate and prices. To get reliability for an asset with a 25 year growing period is very difficult especially as the valuations will be done in a number of economic and commodity price cycles. (company No. 12) — NZ
- (g) Will incur too much time and significant costs for determining quantities as the basis of valuation. It is impossible to examine all trees in our forests, considering the current staff resource. Without examination of each tree, it is impossible to value the forests accurately (The value could be calculated based on selling prices minus felling costs, but timber prices vary depending on grade, type of trees, etc.) We have 457 forests, located in 25 prefectures, 142,000 hectare in total. The cost of examination would be approx. Yen 3,550 million, that is additional wages for hiring part-time staff. Even if we would incur that cost, it is impossible to examine all forests since some forests are inaccessible due to steep slopes. (Company No. 13)

*Asset*

*Asset*

*cost ?*

*Japan forest*



Livestock

- (a) Market prices are determined based on weight per head of cattle. Since 360,000 head of cattle are in a number of locations, with many of the locations inaccessible by road for part of the year, it is impractical to weigh each beast regularly. (company No. 1)
- (b) Therefore, made a reliable estimate of weighs based on the calculated age of the herd in each location. Incurred costs in enhancing the cattle management and accounting systems plus additional staff costs. (company No. 1)
- (c) Incurred costs in enhancing the cattle management and accounting systems plus additional staff costs. (company No. 1)
- (d) No significant problems. It is quite an involved administrative exercise for a company of our size. We have 500,000 + head of cattle on 27 cattle stations covering an area exceeding 13 million hectares. (company No. 3)
- (e) No significant problems/costs. (company No. 6)
- (f) Determining a fair value for the different weights of salmon given the fact that the market price depends also on quality (company No. 11)
- (g) Determining a market price when we have the choice to sell the salmon farmed in Scotland to the industry in Europe, the States or to further process the salmon by ourselves. (company No. 11)

Tea/rubber

- (a) There is no practical market for tea bushes. Costs can be determined reliably from normal historic methods. The biological assets in our case, tea bushes, have a life of over 50 years and, the vagaries of weather can have both significant positive and negative effects on cash flow projections and, therefore, NPV of expected cash flows cannot be reliable - too many subjective assumptions!! (company No. 5) *see Lanka*
- (b) NPV will be the most suitable basis. But net cash flow projections will be highly unreliable due to the long period involved, approx. 20 years. (company No. 15)

Wine/grapes

- (a) An independent valuation on a six monthly basis would cost approx. US\$ 100,000 per year, having some 6,000 hectares of vineyards. May conduct the valuations in-house once the methodology is agreed. (company No. 4)

Sugar

- (a) The only problem relates to the valuation of partly grown cane. For this purpose, a linear representation of biological growth curve was used. (company No. 16 and 17)

### 3. Other comments on biological assets

#### Livestock

- (a) Envisage bang tail musters will need to be completed more regularly to confirm physical quantities. (Company No. 1)

#### Wine/grapes

- (a) A vine is only part of a vineyard. Note that a vineyard consists of land, buildings, trellising, irrigation, water licenses and the vine. (Company No. 4)
- (b) The vineyard is one integral asset and depends on a number of critical components being climate, region, soil characteristics, water resources and physical constraints. (Company No. 4)
- (c) A vine is merely a structure that allows a product to hang from it and does not in itself have much value and is not consumed, unlike a tree, which is physically harvested. (Company No. 4)
- (d) Under AASB 1041, the assets other than vines (such as land, buildings) can be valued at cost while the vine itself needs to be valued at fair value. How can this hybrid calculation result in relevant, reliable, comparable and understandable financial reporting for users? (Company No. 4)
- (e) The difference between the fair value of combined land and biological asset and the raw land gives the improvement value made to the land. This improvement value includes the grape vines (biological asset), but also trellising, irrigation infrastructure, etc. Further analysis of this improvement value is necessary to identify the biological asset value. (Company No.9)

*Aust x 2*

*Aust*

#### Forestry

- (a) Different entities in Australia are taking different approaches to the same issue (e.g. discount rate), hence affecting comparability. From a user perspective, the comparability/reliability could be very misleading. (Company No. 7)
- (b) We are producing hardwood and softwood logs for the saw timber and pulp and paper industries. The growing ages for these products varies from 7 to 30 years. We did not use market price in an active market in its location, as there is no active market of sufficient size to determine market value. (Company No. 10)

*Aust*

*Aust*

#### Sugar

- (a) Used a basis that is not stated in E65: Capitalise the costs associated with land preparation and planting plus carrying costs until bearer biological assets become mature. Amortise over the expected useful life (sugar cane, 5-8 ratoons) (Company No. 8)
- (b) The sugar industry in Guyana is owned by the state. 10% of sugar cane is supplied by independent farmers. The price of sugar cane is set by the State according to a formula which is related to the market price of the end product. (Company No. 16)
- (c) 25% of sugar cane in Papua New Guinea is supplied by independent farmers. The price of sugar cane is set by the State according to a formula which indexes an historic base price to allow for cost inflation. The base price itself was arrived at having regard to smallholder cost and profit margins. The smallholder is free to grow other

*S/Papua*

*Guyana*

*PNG*

crops if he prefers and hence the controlled price approximates to market price.  
(Company No. 17)

#### 4. Comments on fair value used in making business management decisions (Part B: 8)

##### Forestry

- (a) Mostly use cost based information to manage the forestry assets because, having made the decision to be in the forestry business, the key to the business is to maximise margins by minimising costs. (Company No. 7)
- (b) When need to buy/sell forest assets, fair value becomes expected market value in its location. (Company No. 13)
- (c) Some NPV analyses are used to determine whether to stay in or exit the business as a whole and whether to undertake further plantations. However, do not use the fair value data produced for B/S to actively manage the assets. (Company No. 7)
- (d) Moreover, concerned that the management of the payment of dividends and shareholders expectations needs to run counter to the proposals in E65. That is, under E64, unrealised movements in fair values are recognised in the income statement, whereas dividend pay-out policies and shareholder expectations need to be managed on a realised profits basis. (Company No. 7)
- (e) This is one of the decision-making tools used by the company. (Company No. 10)
- (f) The valuation principles are used for some decisions but differing assumptions can be used for different purposes e.g. we view discount rate differently when valuing asset for purchasing new forests: may use discount rate 10-11% rather than 8%. (Company No. 12)

##### Livestock

- (a) For example the fair value of livestock is used to arrive at ROA for each of our cattle properties. The basis for FV is the same. (Company No. 3)

##### Wine/grapes

- (a) The value of the vine itself is not used. Always assessing whether the mix of vineyards is in the best interests of the business and shareholders. The variety, grape end use, quality and fair value or market value of the vineyards is used in this assessment. The value of the vine itself is not used in this exercise. (Company No. 4)

##### Tea/rubber

- (a) Fair value is not used in making business management decisions. But NPV is used as a valuation basis in related situations such as evaluation of future replanting decisions and crop diversification decisions. The associated problems in estimating cash inflows and outflows over a long period is come by using a set of assumptions and recognising associated risks. A sensitivity analysis is also usually done. (Company No. 15)

##### Sugar

- (a) Obviously for return on investment decisions - both for new agricultural investment projects and for purchasing existing farming operations. (Company No. 8)

- (b) We are a vertically integrated business, i.e. Sugar cane plus sugar factory. We measure the returns of the business as a whole and do not seek to measure the separate contributions of field and factory. (Company No. 16 and 17)

Potatoes

- (a) Fair value data are used for making management decisions (e.g. choice of crops). Fair value data are also used for benchmarking among farms. (company No. 18)

## 5. Comments on reporting in the balance sheet (Part B: 9)

### Basis for determining cost

#### - Livestock

- (a) Absorption costing. The costs allocated per head include feed and station running costs. (Company No. 1)
- (b) Livestock will be valued at variable costs related to the livestock, taking account of the age of the animals. This mainly includes feed cost. Normal mortality is also included. (Company No. 11)
- (c) The variable costs consists of brood costs of eggs, landed purchase cost of fish and eggs, landed cost of feed, landed cost of medication, allocation of direct production costs, and cost of fish transport prior to harvest. (Company No. 11)

#### - Forestry

- (a) Cost to establish forest i.e. land preparation, planting, tending, overheads, and interest capitalisation. Use valuation as a cap to cost capitalisation. (Company No. 12)
- (b) For planted trees, costs incurred directly for planting (e.g. land preparation costs). Actual costs are allocated to an individual item based on planting. For purchased forests, purchase amount. (Company No. 13)
- (c) Total tract US\$ 28.3m; land 6m and timber 22.3m. This tract was recently purchased. Since the valuation and purchase price are the same, the tract is currently reported on B/S at cost. (Company No. 14)
- (d) The total cost for the tract was the purchase price and any expenses incurred in completing the acquisition. The cost was allocated over the land and timber products based on value. (Company No. 14)

JS

#### - Tea/rubber

- (a) Cost less accumulated depreciation. Costs incurred on immature plantation. Include material, labour, direct overheads and capitalised borrowing costs. Direct overheads allocated using the percentage of labour used on immature plantations. (Company No. 15)

### Comments by companies that report their assets at fair value

#### - Forestry

- (a) Forests are currently carried at cost subject to impairment testing based on fair value. (Company No. 10)
- (b) An annual valuation is done in terms of the impairment of assets standard. (Company No. 10)

#### - Tea

- (a) The asset is reported at valuation (Land & Development) – Directors valuation based on market price for known transactions involving land & development between

willing buyer and willing seller. The revaluation surplus was credited to undistributable reserves. (Company No. 5)

- Livestock

- (a) We have used fair value in audited F/S as the basis of measurement of livestock and produce at the point of harvest. (Company No. 6) NZ

Other basis

- Wine/grapes

- (a) Valuation (as of 1995) with additions since 1995 at cost. Under AASB 1041, certain to revert to cost for all non current assets. In 1995, vineyards were classified as part of buildings and revalued under the Law, but reclassified into a separate category where compulsory revaluation is no longer required. (Company No. 4)
- (b) Cost of Vines is US\$ 41m, excluding land and buildings. All costs associated with establishing the vineyard are included (e.g. planting preparation and access roads). Vines include rootstock, planting, foliage training and manipulation, soil management, pest and disease control, harvesting, pruning, watering, maintenance etc. Then there is the cost of trellising and irrigation etc. All costs are allocated on a block by block basis. Vineyard improvements to June 1995 are expressed at fair value US\$52m. (Company No. 4) BRL
- (c) Grapes are reported at cost under inventory. (Company No. 4)
- (d) The type of costs included in the cost of grapes are vine amortisation (which includes the initial 4 years of vineyard development consisting of the following costs: rootstock, planting, foliage training and manipulation, soil management, pest and disease control, harvesting, pruning, watering, maintenance, depreciation of trellising and irrigation. All costs are allocated on a block by block basis. (Company No. 4)

## 6. Comments on E65 (Part B: 10)

Opposed to recognition in P/L

- (a) Opposed to recording unrealised gains/losses in P/L. Recognition of unrealised gains may be misleading to users and may lead to dividends on profits that may reverse due to market fluctuations. Recognise increments in value in equity and recycle to P/L when realised. (company No. 1)
- (b) Have strong reservations of reporting fair value changes in P/L (as with AAS 35). (company No. 2)
- (c) If IASC proceeds with E65 as drafted, recognise unrealised gains in equity and transfer to P/L when realised or impaired. (company No. 4)
- (d) Disagree with using a fair value for grapes and reporting part of the total end profit, before the final wine product is sold and the remainder of the profit is reported. Measure grapes at cost. Why is the treatment different from a manufacturer choosing to make a part internally rather than producing it externally? (company No. 4)
- (e) Concerned about the movement into profit and loss account of unrealised gains and losses. This is not good practice and seems to be at variance with generally accepted accounting principles. (company No. 5)
- (f) Not in favour of recognising unrealised gains/losses in P/L. Progress the performance reporting project before starting mandating that fair values be adopted. (company No. 7)
- (g) Measuring biological assets at fair value is a significant change from the historical cost approach. Unrealised gains and losses are being recognised in the Profit and Loss rather than only being brought to account when an arm's length transaction (traditionally a sale) takes place. (company No. 9)
- (h) We propose to sum up the growing stock only in the balance sheet and not in the income statement. This means technically that on the left hand side (assets), we summarize forest stocks in one position and neutralize it on the right hand side (liabilities and equity) under the position "equity". Therefore we propose a separate position inside equity. (company that did not fill in the questionnaire)

Concerned about subjectivity / Doubt reliability

- (a) Allows too much flexibility in determining a "market price" (similar to AAS 35). (company No. 2)
- (b) When no market exists as in tea production (tea bushes) the use of discounted future cash flows becomes an entirely subjective matter. Different enterprises would use different factors/assumptions with implications of comparability of consumers, equity holders or prospective investors. (company No. 5)
- (c) Many biological assets would be more difficult to measure at fair value than investment properties (note that IASC has decided that the difficulties in measuring investment properties warrant an allowed alternative measurement at cost.) (company No. 7)
- (d) Placing a market value on certain biological assets can be subjective due to the number of variables involved in determining a value. An entity's balance sheet may become more difficult to interpret if some assets are measured at cost and others at fair value. Prefer to leave market valuations at an entity/business level rather than at the individual asset level. That is, for a listed company, information on the market value of biological assets should influence a change in the market value of shares

Inventor

Forestry

Grapes

BRL

"

Tea/Rubber  
Sri LankaForestry  
Aust

Grapes

Forestry?  
iForestry  
Aust stateTea/Rubber  
Sri LankaForestry  
AustGrapes  
Aust



rather than force a resulting change through the profit or loss of the company. (company No. 9)

- (e) The theory is fine but the subjective elements in an NPV calculation, significant price fluctuations from year to year used in the NPV calculation over the period of 25 years and lack of reliable transaction data to test valuations makes it too unreliable and would give fluctuating results to an organisation which does not truly reflect the performance over the previous 12 month period. (company No. 12)
- (f) An index, which is used to calculate quantities expected at the time of harvest in the future (for growth and term), is not reliable as a basis of valuation for financial reporting purposes. (company No. 13)
- (g) Subjective features could result in greatly reducing the level of comparability of general purpose F/S among entities. A high degree of comparability between General Purpose Financial Statements of entities in an industry is a fundamental requirement to a vast majority of users of such financial statements. Comparability is important in ascertaining trends and evaluating future performance of entities. (company No. 15)
- (h) Trees are assets that are grown and harvested for a long time. A reliable valuation method is not established for growing trees. (There is no active market.) (company No. 13)
- (i) Support the remarks by the Dutch NIVRA that the valuation at fair value of biological assets like a 3 year old fruit tree plantations (where active markets are not available) is problematic. A net present value calculation is difficult and it is unclear why the profit from future years should be discounted and treated as the value of the trees (and not as the value of other assets). (company No. 18)

Forestry  
NZ

Forestry  
Japan

Tea

Forestry  
Japan

Potatoes  
Netherlands

#### Propose a different model from E65

- (a) Measure developing vineyards (including vines) at cost, as they do not reach commercial maturity until the end of 4 years. Measure currently developed vineyards at cost or market value with the revaluation increment in equity under a revaluation reserve. (company No. 4)
- (b) Allow to report physical changes in operating profit and price changes in a second performance statement. (company No. 6)
- (c) Measure biological assets at the lower of cost or net realisable value for reporting purposes. The same should apply to agricultural produce (profit is brought to account when produce is sold) (company No. 8)
- (d) Measure biological assets and agricultural produce at the lower of cost or net realisable value, especially when the period between initiation and harvest is relatively short. (company No. 11)

Grapes  
Bel

Wool NZ

Sugar  
S/Africa

Sulman

#### Significant costs would be incurred

- (a) Compliance would impose significant additional costs to more frequently gather all of the inventory and local market information for our entire timber portfolio, as well as additional audit costs. (company No. 14)

Forestry  
US

#### Mature/immature

- (a) We propose that the differentiation of the forest stocks into "mature" and "immature" is not sensible. In fact it's no objective aspect, if a stand is ready for cutting or not. Take for example an oak stand (80 years): One can use it for fuel wood = mature or

leave it in order to produce high quality (vener) = immature. (company that did not fill in the questionnaire)

Favour E65

- (a) By measuring livestock at FV, (a) our operating result correctly reflects the market for our product (realised and unrealised) and the operations of the company, (b) our B/S more accurately discloses net worth of the company. (company No. 3)
- (b) Fair value is more relevant for enterprise stakeholders (including management, creditors, directors and shareholders) than any other known basis of measurement, and it is reliable. In particular it is more accurate and objective than historical costs (given the subjectivity in allocating joint costs). (company No. 6)

Lucembourg  
Aust

Wood  
NZ

Other comments

- (a) Establish significant further guidance before true comparability of financial reporting (rather than mere apparent harmonisation) is achieved. One way could be to issue the Standard with a long lead time (e.g. 3 years) to its operative date and to establish industry working parties to identify and resolve the issues prior to the operative date. (company No. 7)
- (b) The transitional provisions in E65 are grossly unfair, in that they force an enterprise to take the initial increment to fair value directly to retained earnings and the unrealised profit at adoption will never be recognised in income or EPS. The enterprises with long production cycles (such as forest growing) would be forced to endure lower reported income for many years. In our case, the impact on profits over the next 15 years is estimated to be in the vicinity of 15-20%. In the case of major paradigm changes such as E65, transitional provisions should be used to help mitigate the economic impact of new requirements and ensure the new requirements can be adopted without overly penalising the enterprises that adopt the Standard. (company No. 7)
- (c) Do not believe our long-term investors need quarterly or annual market valuations on timber assets, which are generally held for 25 to 50 years. Concerned that an accounting standard, and subsequent interpretations from accounting and regulatory authorities would not provide the flexibility we would need to provide useful information for investors. (company No. 14)
- (d) Commercial agriculture is merely another business activity and there is no reason, and certainly the exposure draft fails to produce any valid reasons, why its assets and profitability should be measured on a unique basis. Indeed the result could well be disastrous for the sector by making it appear an unattractive investment compared to other commercial enterprises. The reasons why Bank and Insurance Companies have different accounting treatment do not apply to commercial agriculture concerns and it would only confuse the user of the accounts. (company No. 5)
- (e) The valuation of forestry biological assets is not consistent which makes difficult to compare the results of within the industry. (company No. 10)
- (f) E65 is in conflict with the overall IASC Framework which states that F/S should be prepared in accordance with an accounting model based on recoverable historical costs. (company No. 11)
- (g) If IASC go down this track will the U.S. follow and if they don't this will be another significant difference between USGAAP and the other jurisdictions. (company No. 12)

Forestry  
Aust

Forestry  
Aust

Forestry  
US

Ten/Rubber  
Sri Lanka

Forestry  
?

Salmon  
Aust

Forestry  
NZ

- (h) AASB1037 was issued despite the constructive suggestions by the respondents. Hope the results of this field test provide valuable information on which a workable accounting standard can be developed. (company No. 1)
- (i) In Australia, a fair value approach will be required for financial years ending 30 June 2001, and the company is investigating the merits of adopting the standard early. (company No. 1)
- (j) We value its grape vines at fair value because there is an Australian accounting standard that requires this measurement basis. (company No. 9)
- (k) No problem with agricultural produce. Forest assets are sold immediately after harvest in general and profits/losses are recognised at that time. (company No. 13)
- (l) Propose requiring companies to produce additional statements restating assets and results under E65 during an initial period. These statements could be assessed and a decision could be made at a later date if ED65 provisions are to be converted in to an IAS. (company No. 15)
- (m) We would see measurement at cost as an equally valid alternative for sugar cane as measurement at fair value. However, from an internal accounting perspective, the fair value method would be preferred for its simplicity. (company No. 16 and 17)
- (n) By accounting for sugar cane at fair value, we will continue to allow costs to be expensed as incurred. This encourages clarity of expression and facilitates cost control. (company No. 16 and 17)

*livestock  
Aust*

*v*

*Wine s'cap*

*Forest Sugar*

*Tan/Rubber*

*Sugar*

*Sugar*

*Guyana / 1986*

## **Appendix 16: Two Media Comments on AASB 1037**

### **'New Controversies Wrack Standard-Setting Scene'**

Corporate unease over the standard on living things - AASB 1037: Self-Generating and Regenerating Assets (SGARA) - was highlighted by Rick Allert, Chairman of one of Australia's biggest wine producers, Southcorp Holdings. At a recent lunch meeting of the Institute of Chartered Accountants in Australia held in Melbourne, Allert lashed out at the new standard, saying that it would inflate profits, especially in the first year, and alienate US investors.

"A key Southcorp market is the US, where institutional investors are notoriously suspicious of anything which makes accounts more opaque or which appears to inflate the results of non-US companies," he said.

The standard at the centre of Allert's complaints, due for adoption on 1 July, requires companies with assets of grape vines, growing crops, orchards and cattle to value the assets at market value on balance day and bring any unrealised gains or losses into the profit and loss account. As a result, and in Southcorp's case, the profits from a grape crop are brought to book as they grow, and not when the grapes are picked and made into wine - possibly many years later.

Allert said he did not see why Australia had to lead the rest of the world in setting such a standard - he believes it is too small a country to be a leader in such matters. He also wondered why Australian standards could not simply be the same as US GAAP.

Australian Accounting Standards Board chairman Ken Spencer was quick to defend the standard, pointing out that the IASC is developing its own standard on the same issue, which draws heavily on the Australian version. He said Australian standard-setters had consulted closely with their leading overseas counterparts and there was broad agreement on the approach. He also rejected any suggestion that capital markets would be confused over the new standard which, he noted, leads to only a speedier recognition of revenue earned from grapes.

The standard should also overcome the anomaly, when using the historical cost method, of valuing the picked grapes a company grows on a different basis from the grapes it buys in, he added.

**Source:- The Accountant, London; 1 April 1999**

### 'Money Does Grow On Trees – Now' by Leon Gettler

How much money grows on trees? How much of a cash cow is that Holstein-Friesian calf?

For the past two years, a war has raged between accountants and industry over these and other seemingly esoteric questions.

To the bean counters, it made sense putting the goose that laid the golden egg on the balance sheet. They saw valuations creating a level playing field and allowing investors to compare apples with apples.

And because there was no international standard on living assets, they said, it was only fitting that a country such as Australia with a strong agricultural sector would lead the world in standard setting.

But industry said that only a bunch of accountants could think like that. And only an accountant, they said, would think of sticking a value on something like a calf that had not yet generated value.

For industry, the problem was getting primary producers to recognise unrealised gains that may not be realised as profit for many years. But in the end, the accountants won.

Under a new accounting standard that takes effect today, all living assets will go on the balance sheet. The standard for "self-generating and regenerating assets" - **SGARA** to accountants, but crops, forests, fruit-bearing trees, fish and other livestock to everyone else - was to have been introduced this time last year.

The exercise was aimed at allowing a comparison by requiring companies to put a market value on those assets and declaring any changes. This meant giving SGARAs a net market value each reporting date. The net market value of a calf, for instance, might be determined by the most recent net market price being fetched at the time, the net value of related assets, the net present value of discounted cashflows that the calf was expected to generate and costs such as feeding and drenching.

The result: corporate uproar that caused the standard-setting authorities to defer it for 12 months.

Southcorp was particularly scathing about the changes, claiming they would damage the wine industry. Southcorp's executive general manager of corporate affairs, Glen Cunningham, said the accounting treatment distorted the real picture in the accounts.

"It means you're reporting something that's further away from the actual cashflow," Mr Cunningham said. "Secondly, in a globalised world, we should not be seen as leading the accounting standards. We should be harmonising them instead. Finally, there is a high level of compliance cost."

But the CPA Australia director of accounting and audit, Colin Parker, said a clear set of rules would allow comparisons across a range of assets.

"You can't cherry pick accounting standards," Mr Parker said

**Source:- The Age, Melbourne; 3 July 2000**

### **Appendix 17: AASB – Respondents to ED 114 – ‘Agriculture’**

- Sub 1 Queensland Department of Primary Industry – Forestry
- Sub 2 Ian Langfield-Smith - Monash University
- Sub 3 J.B. Ryan – University of Western Sydney
- Sub 4 Pitcher Partners
- Sub 5 Keith Alfredson – N.B. As a private individual
- Sub 6 Forest Products Commission, West Australia [FPC]
- Sub 7 Group of 100 Inc. [G-100]
- Sub 8 Deloitte Touche Tohmatsu
- Sub 9 Athol J Warman
- Sub 10 Foster’s Group Ltd
- Sub 11 Australasian Council of Auditors-General - ‘Auditors-General’  
 Submitted by the Tasmanian Audit Office - representing the Auditors-General of New South  
 Wales, Queensland, West Australia, Tasmania and the Northern Territory.
- Sub 12 Tasmanian Heads of Treasurers Accounting & Reporting Advisory Commission  
 [HoTARAC]
- Sub 13 Forestry Tasmania
- Sub 14 Institute of Chartered Accountants in Australia [ICAA]
- Sub 15 Ernst & Young

#### **Responses on ED 114 and on other Exposure Drafts**

- Joint Sub 1 Prof. Graham Peirson - Monash University
- Joint Sub 2 BHP Billiton Ltd
- Joint Sub 3 Woodside Petroleum Ltd
- Joint Sub 4 KPMG
- Joint Sub 5 PricewaterhouseCoopers

**Source:** Australian Accounting Standards Board

Exposure Draft ED 114 - Request for Comment on IAS 41 ‘Agriculture’

List of Submissions received

**Appendix 18: NZICA – Respondents to ED-90: Agriculture**  
**‘Comment on IAS 41 Agriculture’**  
**List of Respondents in Order of Submissions**

**Member Bodies and Other Accounting Bodies**

[23]	ICANZ Head Office - National Practice Committee	David Barker
[17]	ICANZ Institute – Hawke’s Bay Branch	Giles Pearson
[53]	ICANZ Institute – Hawke’s Bay Branch	Janice H Atkinson
[22]	ICANZ Institute – Manawatu Branch	Sheena Mason
[05]	ICANZ Institute - Southland Branch	Bruce D Kooman
[15]	ICANZ Institute – Taranaki Branch	Stephen Waite
[57]	ICANZ Institute – Waikato/Bay of Plenty Branch	Elizabeth Hunter
[79]	ICANZ Institute – Waikato/Bay of Plenty Branch	Phillip Price
[24]	ICANZ Institute – Wairarapa Branch	Syd Morgan
[07]	ICANZ Institute – Wanganui Branch	P. R. Lundrum

**Accounting Firms/Accountants**

[62]	Ernst & Young	D. A. Jackson – Partner		Auckland
[32]	KPMG	(Matt Prichard – National Technical Director		Wellington
[83]	PricewaterhouseCoopers	Warwick E. Hunt – Partner		Auckland
[90]	Bain & Sheppard	Bill Harding	Gisborne	Pub Accts
[03]	B H Maxwell & Co Limited -	Brian Maxwell, FCA	Timaru	Pub Accts
[47]	Carey Smith & Co	Murray Carey	Wanganui	Pub Accts
[18]	Chapman Giller Roe Limited -	Dean Roe	Taupo	Pub Accts
[26]	Cleal & Christian	David Cleal	Featherston	Pub Accts
[04]	Croys Limited	Trevor Croy	CA Ashburton	Pub Accts
[11]	Cronin Cullen Egan Limited -	Graham Cullen	Tauranga	Pub Accts
[98]	CST Management Limited –	B. H. Sole	Manukau	Pub Accts
[20]	Dockrill Mitchell McCleary -	Russell Dockrill	Timaru	Pub Accts
[70]	Dockrill Mitchell McCleary -	A.T. McCleary	Timaru	Pub Accts
[72]	Dockrill Mitchell McCleary -	Dean Mitchell	Timaru	Pub Accts
[76]	DPA & Associates	Paul Wilson	Taupo	Pub Accts
[27]	Geenty Walsh & Partners -	G. R. Geenty	Hastings	Pub Accts
[21]	Graham & Dobson		Gisborne	Pub Accts
[28]	Graham & Dobson	Graham C. Rosie	Gisborne	Pub Accts
[64]	Graham & Dobson	David Quinn	Gisborne	Pub Accts
[48]	Gregor Vallely		Wanganui	Pub Accts
[80]	Gresham Walkinton & Co Ltd -	R. Walkinton	Wanganui	Pub Accts
[84]	Ibbotson Cooney Limited		Alexandra	Pub Accts
[43]	Iles Casey	D. E. Bufton	Rotorua	Pub Accts
[36]	Jordan Horton & Co Limited –	E. Jordan	New Plymouth	Pub Accts
[34]	Malloch McClean -	Patrick A. Houlihan	Gore	Pub Accts
[77]	McCullochs	L. P. Evans	Gisborne	Pub Accts
[89]	McCullochs	D. M. Keast	Gisborne	Pub Accts
[12]	Meredith D Lowe & Associates		Ashburton	Pub Accts
[85]	Peters Doig - Mark Peters for NZ Wine Co Ltd		Blenheim	Pub Accts
[14]	Ryan Thomas & Co	A. Thomas	Taihape	Pub Accts
[39]	Sadler Oakly Newman Limited –	A. W. Newman	Masterton	Pub Accts
[88]	Stretton & Co Ltd –	S. Bignell/T Palmer/G. White	Taupo	Pub Accts
[40]	Waite & Blackburn	S. R. Waite	Inglewood	Pub Accts
[35]	Ward Wilson Limited	R. Paul Checketts	Invercargill	Pub Accts

[46]	West Yates Limited	G. Hosie	Nelson	Pub Accts
[30]	Wilson Stafford-Bush - Stephen Stafford-Bush		Waiuku	Pub Accts
[68]	Wood Watson	Peter Wood	Tauranga	Pub Accts
[54]	Kerry G. Adams		Christchurch	CA
[59]	Kathryn de Bruin		Dargaville	CA
[55]	Paul Hickson		Te Puke	CA
[99]	B.A. Monopoli (ICANZ Primary Sector Committee)		Richmond	CA
[19]	Colin Oleson		Te Puke	CA

### **Industry Representative Groups**

[97]	AgResearch Limited - C Leo Bourke – CFO			Hamilton
[75]	Federated Farmers of New Zealand Inc - James Ryan + Survey of 500 members			
[61]	NZ Horticultural Economic Service - Mike Kearney		Nelson	
[50]	Gisborne Grape Growers Society			Gisborne
[56]	Katikati Fruitgrowers Assn.	D. Zonderop		Katikati
[58]	The Hawke's Bay Fruitgrowers Association [+101 Growers]			Hastings
[100]	Green Growers Association Inc -	David Watts	Kiwifruit	Katikati
[51]	Pukekohe Vegetable Growers Assn -	Glenn Hunter		Pukekohe
[91]	The National Organisations for Fruit and Vegetable Growers - Peter Silcock			
[71]	NZ Institute of Forestry Inc - Alan Barnes	Forestry Valuations		Rotorua

### **Industry & Commerce – Agricultural Entities – Non-Bearer SGARAs – Private Sector**

[31]	Carter Holt Harvey - Jonathan P. Mason - CFO		Forests	
[41]	Evergreen Forests Limited - Vivek Singh - CFO		Forests	
[49]	Fletcher Challenge Forests - John Dell – CFO		Forests	
[81]	Forest Enterprises Limited – A. Wilton		Forests	Masterton
[73]	Gerard Archbold, CA Forestry Company		Forests	Gisborne
[44]	Mangatu	Jim Campbell – CFO	SGARA General	
[69]	Mt. Aspiring Station -	John Aspinal	SGARA - Sheep Cattle Bees	
[29]	Oldershaw & Co Limited – N. D. Edmundson		SGARA Enterprises Napier	
[25]	K. Ellis [& 6 others]		Vineyards/Orchards/Farmers	
[01]	A. S. Wilcox & Sons Limited – E. K. Gillott - CFO		Crop	Pukekohe
[02]	A. S. Wilcox & Sons Limited – B. C. Bain Fin Accountant		Crop	Pukekohe
[37]	Landcorp Farming Limited - A. J. Johnson		Livestock	Wellington
[38]	Parinihi Ki Waitotara Inc - P. Charleton - CEO		Cattle	Stratford
[52]	Tahora 2C2 Section 2 - Jim Campbell CA, Fin Controller		Farming	Gisborne
[60]	Lowcliffe Farm	Elwyn Smith	Farmer	Ashburton
[08]	L. E. Mullany		Farmer	Tolaga Bay
[09]	Mavis Barwick		Farmer	Te Karaka
[10]	Gene & Therese Williams		Farmers	Gisborne



**Industry & Commerce – Agricultural Entities – Bearer SGARAs**

[13]	Montana Wines Limited	Rob Aitken	Vines	Auckland
[86]	The New Zealand Wine Co. Ltd.	John Milne	Vines	Blenheim
[16]	Villa Maria Estate Limited	Martin Jackson	Vines	Auckland
[33]	Johnny Appleseed Ltd - Sandra Bostock – GM Finance		Horticulture	Hastings
[42]	Allan Baldock – Grower		Horticulture	Hawkes Bay
[87]	Collective Submission - 21 CAs – E. Cooper		Kiwifruit	Bay of Plenty

**Public Sector**

[96]	Audit New Zealand	A.E. Boulton – Technical Director		
[95]	Office of the Auditor-General	Kevin Brady		
[45]	Ministry of Agriculture and Forestry - Garry Herrington – Senior Policy Analyst			
[92]	Securities Commission	Joanne Moores – Senior Executive		
[94]	The Treasury	Ken Warren for The Secretary		

**Academics**

[78]	Lincoln University, Centre for Accounting & Research - Murray Clark + 4 others)			
[06]	The Open Polytechnic of NZ	D. H. Bourke		Lower Hutt
[74]	Unitec Institute of Technology	Richard Woolf + 8 others		

**Valuers**

[67]	Barry Murphy - CA	P.F. Olsen Group Consultant	Forest Valuer	
[66]	Infrastructure Auckland	Peter Casey	Valuer	Auckland
[63]	New Plymouth District Council - Graeme Trevathan		Forestry JV & Valuer	

**Other**

[65]	Burnard Bull & Co	Solicitors		Gisborne
[82]	Federation of Maori Authorities	Paul Morgan		
[93]	New Zealand Law Society	Simon McArley – Commercial & Business Law		

**Source:** New Zealand Institute of Chartered Accountants.

List of Original Submissions received to ED-90: *Agriculture* - Comment on IAS 41 'Agriculture'.

## Appendix 19: Foster's Group Limited - Letter to AASB Chairman

FOSTER'S GROUP LIMITED  
 77 Southbank Boulevard Southbank Victoria 3006 Australia  
 Tel 61 3 9633 2053 Fax 61 3 9633 2066 email trevor.ohoy@fostersgroup.com  
 ABN 49 007 620 886

Trevor L O'Hoy  
 Senior Vice President & Chief Financial Officer

23 August 2002



Mr Keith Alfredson  
 The Chairman  
 AASB  
 P O Box 204  
 Collins Street West  
 MELBOURNE VIC 8007

Dear Keith

### **SGARA accounting standard change**

Foster's believes that the agriculture accounting standard should be adjusted to exclude the impact of this standard on the wine industry.

Foster's Group Limited ("Foster's") has now had three years experience with reporting in accordance with the requirements of AASB 1037 "Self-generating and regenerating assets" ("SGARA"). During this time, Foster's has participated in the IASC field study on agriculture and provided feedback on the practical implementation issues of SGARA. This feedback assisted the IASC to develop IAS 41 "Agriculture" which applies from 1 January 2003.

Given the depth of experience, Foster's has concluded that the accounting requirements and valuation concepts of SGARA when applied to a wine business are too complex for the average user (including analysts) of financial statements to understand. Businesses involved in the wine industry produce and market wine and in general, they do not trade in living assets. The analysts of a wine business tend to focus (quite correctly) on cash performance, particularly given the capital intensive nature of the wine industry. Adding the valuation of living assets into the financial results of a wine business makes the cash analysis unnecessarily difficult. As an example, SGARA revenue does not equal the non-cash adjustment required in a reconciliation of cash to operating profit due to the amortisation of prior period expenses capitalised in inventory.

Consistent with the financial results announcements of other major Australian companies in the wine industry, Foster's now presents its financial results to the investment analysts excluding the effects of SGARA. It has taken a number of years for the analysts to understand the unique SGARA accounting requirements, which has resulted in constant questioning of Foster's senior management to explain the impact on the financial results. To assist their understanding of the financial impact, Foster's releases the forecasted future year financial impact of SGARA. The analysts seek to reverse the SGARA EBITA impact from inventory, thereby reverting inventory back to historical cost.

If the investment community reverses out the impact of SGARA to perform financial analysis on the results of wine businesses, we must ask ourselves what purpose this standard serves. At the vineyard level the business is still managed on a cost of production basis (ie. cash cost). The inventory costing system excludes SGARA. The business merely incurs additional expense from valuers, accountants, auditors, tax specialists, and management in determining and understanding the impact of SGARA.

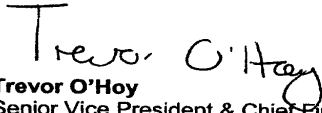
- 2 -

The wine industry regards its vines as more akin to equipment which must generate an annual return, rather than say immature pine trees, which will eventually turn into saleable assets as mature pine trees.

Foster's therefore believes that the agriculture accounting standard should be adjusted to exclude the impact of this standard on the wine industry. As a suggestion, the SGARA standard could be exempt from applying to integrated businesses that apply value adding processes to agricultural produce (eg. a wine business that converts its own grapes into wine).

Foster's would welcome the opportunity to meet and discuss these comments further and would be willing to participate in discussions to further develop or clarify this standard.

Yours sincerely



**Trevor O'Hoy**  
Senior Vice President & Chief Financial Officer

**Foster's Background**

Foster's is a premium branded beverage company and is affected by AASB 1037 through the vineyards owned by the Group's Wine division. Foster's relies on its own vineyards to source approximately 30% of grapes used in the production of wine which, as living assets are measured at net market value. The majority of this net market value impact is from the growth of grapes as vines as a rule are not commonly traded. The valuation increment from picked grapes is capitalised into the carrying value of wine inventory and only released into the profit and loss when the wine is sold, which may be up to three years after harvest. //

Cc: A Thompson – AASB

## Appendix 20: Delahunty Trust Project Interviewees

### Users

ABN-AMRO	D. Cooke – Director – Equities	Sydney, NSW
ANZ Corporate Banking	E.A. Hore – Snr. Analyst:- Agribusinesses	Melbourne, Vic.
Credit Suisse First Boston	L. Gandler – Director, Australian Equities Research	Melbourne, Vic.
J.B. Were Research	P. Ryan – Industrial Research	Melbourne, Vic.
J.P. Morgan	S. Jackson	Melbourne, Vic.
National Australia Bank	D. Watts – National Executive, Credit Risk Manager	Melbourne, Vic.
Standard & Poor's	J. Ward - Director Rating Services	Melbourne, Vic.
	L. Kistler – Rating Specialist	Melbourne, Vic.
Westpac Institutional Bank	D. Gorman – Director, Consumer Industry Group	Sydney, NSW
	A. Macgonigal – Associate, Corporate Securities	Sydney, NSW

### SGARA Preparers

Atlas South Sea Pearl	S. Adams – GM Corporate & Finance, Co. Secretary	Perth, WA
BRL Hardy Limited	P.M. Beckwith, Group Financial Director	Adelaide, SA
Cape Mentelle Vineyards	I. Mayo, General Manager, Finance & Administration	Perth, WA
Forest Enterprises Group	M. Matthews, Financial Controller	Launceston, Tas.
Forest Products Commission	D. Oelofse, Financial Accountant	Perth, WA
Fosters Limited	T. O'Hoy, Chief Financial Director	Melbourne, Vic.
	P.G. Smith – Strategic & Corporate Finance	Melbourne, Vic.
Pipers Brook Vineyard	S. McKay, Financial Controller	Launceston, Tas.
Southcorp Limited	D.J. Jeffries – General Manager Accounting	Magill, SA

### Auditors & Accountants

Deloitte Touche Tohmatsu	B.C. Porter – Partner, Technical.	Melbourne
Deloitte Touche Tohmatsu	R. Whitehead, Partner	Launceston, Tas.
	S. Heryk, Partner	Launceston, Tas.
Ernst & Young	R. Picker - Partner, National Accounting & Auditing Standards [and Acting-Chairman AASB]	Melbourne
	J. Davies – Partner	Melbourne
KPMG	K. Peach – Partner	Melbourne
KPMG	K.N. Dean, Partner	Hobart, Tas.
	A. Gray, Senior Manager	Launceston, Tas.
PricewaterhouseCoopers	A. Mill – Partner, Consumer & Industrial Products	Melbourne, Vic.

### Others

AASB	A. Thomson	Technical Director	Melbourne, Vic.
Australian Financial Review	S. Evans	Journalist	Melbourne, Vic.
University of Tasmania	B. Williams	Research Student	Launceston, Tas.
University of West Australia	A. Tarca	Lecturer	Perth, WA
University of West Australia	R. Newby	Lecturer	Perth, WA
WA Dept. Treasury & Finance	J. Stanley – Principal Financial Advisor, Accounting Policy		WA

**Source:** J.H.G. Milne during October 2002 and July 2003.

## Appendix 21: AASB PIR Letter to IASB Chairman

AASB 10-11 December 2003  
Agenda paper 15.4



AUSTRALIAN  
ACCOUNTING  
STANDARDS  
BOARD

PO Box 204  
Collins St West Vic 8007

Telephone: (03) 9617 7600  
Facsimile: (03) 9617 7608

25 November 2003

Sir David Tweedie  
Chairman  
International Accounting Standards Board  
30 Cannon Street  
LONDON EC4M 6XH  
UNITED KINGDOM

Dear David

### **IAS 41 Agriculture: Recommendations**

In its process of adopting the standards of the IASB, the AASB is issuing a series of Exposure Drafts, containing proposals for the equivalent Australian standards. Following consideration of submissions received on an ED, the AASB will advise the IASB of the outcome and recommend amendments to IASB standards aimed at enhancing the clarity and effectiveness of the IASB set of standards.

Exposure Draft ED 114 *Request for Comment on IAS 41 Agriculture* proposed that IAS 41 be adopted without amendment even though a number of differences exist between IAS 41 and the current Australian Standard dealing with agriculture, AASB 1037 *Self-Generating and Regenerating Assets*. After consideration of the submissions received on ED 114 the Board decided to continue with its proposal to promulgate an Australian equivalent of IAS 41. However, two additional disclosure requirements currently included in AASB 1037 will be carried forward in the Australian equivalent of IAS 41. These disclosures relate to:

- **Physical quantity categories** – Both AASB 1037 paragraph 7.1(a) and IAS 41.46(b) require disclosure of physical quantities of SGARAs. AASB 1037 paragraph 7.1(a) requires that the physical quantity of SGARAs be categorised as plants or animals, with additional sub-classifications, as appropriate. For example, the sub-classification of plants and animals showing separately those SGARAs over which the entity has rights that are obtained through leases or similar types of arrangements is required. In contrast, IAS 41.43 notes that the physical quantities may be distinguished between consumer and bearer biological assets or between mature and immature biological assets, as appropriate. The Australian equivalent of IAS 41 will insert the requirement:

*“An entity shall disclose the nature of biological assets and an estimate or relevant indication of their physical quantity, separately classified between ‘plants’ and ‘animals’, and sub-classified as appropriate to the circumstances of the entity, showing separately those biological assets subject to a lease arrangement.”*

- **Restrictions** – AASB 1037 paragraph 7.1(b) requires disclosures where the entity's use or capacity to sell SGARAs is restricted. The total and restricted amounts of those SGARAs must be disclosed, together with details of the nature and extent of those restrictions. IAS 41.49(a) only requires disclosure of the amount of biological assets subject to restrictions. The Australian equivalent of IAS 41 will insert the requirement:

*“An entity shall disclose biological assets for which the entity's use or capacity to sell is subject to restrictions imposed by regulations or other external requirements that have a significant impact on their total fair value less estimated point-of-sale costs. The total and restricted amounts of those biological assets shall be disclosed, together with details of the nature and extent of those restrictions.”*

We trust the IASB will consider adding these disclosures to IAS 41 when IAS 41 is next amended.

#### **Post Implementation Review of AASB 1037 / AAS 35 and IAS 41 Convergence Issues**

The AASB staff recently undertook a post implementation review of the requirements of AASB 1037 / AAS 35. This review also addressed potential convergence issues with IAS 41.

IAS 41 became operative for the first time for financial years beginning on or after 1 January 2003 and difficulties in implementing IAS 41 have not yet been identified. In contrast, many Australian companies with self-generating and regenerating assets have had experience in applying the requirements of AASB 1037 for 3 financial years, with AASB 1037 becoming operative for financial years ending on or after 30 June 2001.

The purpose of the review was to establish which standard is superior and whether either or both standards require review in the short term and in the longer term. The AASB Strategy Paper on the post implementation review and a collation of the responses received are enclosed for the IASB's consideration. Please note, that for confidentiality reasons, the collation of responses is not to be distributed beyond IASB members and staff.

The responses from the post implementation review indicated that many Australian entities expect that they will apply the same valuation technique under the Australian equivalent of IAS 41 as they apply under AASB 1037 and consequently do not expect additional problems. Although the measurement requirements in both AASB 1037 and IAS 41 are substantially the same, one respondent pointed out the ambiguity in the interpretation of IAS 41 paragraph 21, specifically whether, consistent with the requirements of AASB 1037, the potential for future growth should be included in the valuation. We understand that the interpretation of IAS 41 paragraph 21 is currently being addressed by the IFRIC.

Despite entities believing that additional problems will not be encountered in applying IAS 41, entities in particular industries or with special features reconfirmed previous feedback to the AASB regarding the perceived inappropriateness of SGARAs accounting under AASB 1037 (and IAS 41) to the entity. These entities believed that the cost outweighs the benefits of accounting in accordance with AASB 1037 (or IAS 41). The special features identified were:

- **Wine companies** – Many wine companies run a vertically integrated operation from the growing of the grapes through to the distribution of the wine. Some of these companies consider that SGARAs accounting requires them to recognise profits or



losses prematurely, from the stage when the grape growing occurs, even though the grapes from which the wine is made may not effectively be sold for a number of years. This means that an entity is reportedly exposed to accounting for its vines and grapes in accordance with the SGARAs accounting requirements. However, they believe that the information is of no benefit because one of the purposes in creating a vertically integrated operation is to reduce exposure to external factors.

- **Bearer SGARAs** – Some entities believe that application of fair value measurements to annual crops or products with short life cycles is not appropriate. During a twelve month period the actual revenue for sale of the harvest can usually be identified. SGARAs accounting simply brings forward recognition of that revenue using a less reliable measurement technique than actual proceeds of sale. The long-term bearer-SGARA upon which annual crops are grown (e.g. grapevines or fruit trees) are believed to be akin to equipment and should be carried at cost and depreciated under the requirements of IAS 16 *Property, Plant and Equipment*. It is believed that by excluding bearer SGARAs from the scope of the IAS 41, the rebuttable presumption in IAS 41.30 that allows biological assets to be carried at cost less accumulated depreciation and accumulated impairment losses when the fair value of the biological asset cannot be measured reliably could also be removed from the Standard.
- **Small companies** – Small companies believe that the cost of SGARAs accounting does not provide great benefit to the users of the information. This issue may be addressed by the IASB's Small and Medium Entities project.

Based on the feedback received in the post implementation review, the AASB project staff recommend the following changes to IAS 41:

- **Scope of standard** – The AASB project staff believes there is merit in excluding bearer SGARAs and entities with vertically integrated operations from the scope of IAS 41 for the reasons stated above.
- **Leases involving SGARAs** – The AASB project staff believes that AASB 1037 contains superior requirements regarding leases involving SGARAs than the requirements in IAS 41. The differences in the leasing requirements between AASB 1037 and IAS 41 are:
  - **Operating leases of SGARAs** – Under IAS 17 *Leases* paragraph 25, a lessee of a biological asset does not recognise an asset but instead recognises the operating lease payments as an expense. In contrast, where an operating lease gives the lessee an exclusive right over SGARAs, AASB 1037 paragraph 2.1(b) requires the lessee to recognise and measure that right at its net market value, as if that right is itself a SGARA.
  - **Leases of SGARAs** – In respect of leases covering exclusive rights over SGARAs, AASB 1037 paragraphs 2.1(b), 5.2 and 5.3 require that:
    - where a finance lease gives an exclusive right over a SGARA, the lessee recognises and measures that right as if that right is a SGARA; and
    - where a lessor leases a SGARA under an operating lease, the lessor recognises and measures that right as if that right is a SGARA.

For leases giving non-exclusive rights over SGARAs, there are no specific requirements in Australian GAAP because these leases are excluded from AASB 1008 *Leases* (paragraph 2.1(a)).

IAS 17.1 states that IAS 17 does not apply to:

- lessees of biological assets held under a finance lease; and
- lessors of biological assets leased under an operating lease.

It follows that, unlike IASB GAAP, Australian GAAP contains “specific” requirements about leases of biological assets conveying exclusive rights. In some circumstances Australian GAAP and IASB GAAP would require a lessor to apply lease accounting in respect of operating leases covering non-exclusive rights over biological assets controlled by the entity.

- **Disclosures** – Many respondents consider that IAS 41 contains requirements to disclose information that is seen to be commercially sensitive. This would include separate disclosure of (for a wine company):
  - the aggregate fair value increment and decrement for grape vines (IAS 41.40);
  - the net increment or decrement relating to grape vines only (IAS 41.50); and
  - net fair value of grapes harvested during the period (IAS 41.48).

Using these disclosures, the vineyard costs (the commercially sensitive information) could be identified by deducting the increment / decrement relating to grapes from the fair value of those grapes. It is recommended that the disclosure of the reconciliation of changes in the carrying amount of biological assets between the beginning and end of the reporting period (IAS 41.50) is removed from IAS 41.

As mentioned above, the AASB has decided the Australian equivalent to IAS 41 will include additional disclosure requirements relating to physical quantities and restrictions on title of SGARAs that will be carried forward from AASB 1037. The AASB recommends that these are incorporated into IAS 41.

We urge the IASB to consider the comments as soon as possible with a view to the IASB undertaking a comprehensive review of the IAS 41 requirements. The AASB is willing to assist in this review.

Yours sincerely



**Monique Ledden**

Project Manager - Australian Accounting Standards Board  
 Level 3, 530 Collins St. MELBOURNE Victoria 3000  
 ☎ 61 3 9617 7631 Fax: 61 3 9617 7681 Email: [mledden@aasb.com.au](mailto:mledden@aasb.com.au)  
 <<mailto:mledden@aasb.com.au>>

Enc.



**Appendix 22A: AASB Post Implementation Review**  
**Strategy Paper for PIR Questionnaire**

AASB Meeting 2-3 September 2003  
 Agenda paper 6.5.2

**Self-Generating and Regenerating Assets  
 Post Implementation Review – Strategy Paper  
 May 2003**

(Last updated August 2003)

**Introduction**

Based on the proposals in the AASB's ED 114 "Request for Comment on IAS 41 Agriculture", entities that are currently applying AASB 1037 / AAS 35 "Self-Generating and Regenerating Assets" (SGARA) will need to comply with the requirements of IAS 41 "Agriculture" for financial years beginning on or after 1 January 2005.

IAS 41 became operative for the first time for financial years beginning on or after 1 January 2003. We are not aware of any entities early adopting the requirements of IAS 41 and difficulties in implementing IAS 41 have not yet been identified.

Foster's Group Limited wrote to the AASB (letters dated 23 August 2002 and 10 December 2002) expressing its view that AASB 1037 / AAS 35 should be amended to exclude the impact of the standard on the wine industry (a Bearer-SGARA industry). This is on the basis that the accounting requirements and valuation concepts when applied to a wine business are too complex for the average user of financial statements to understand and that the major performance measure is based on the entity's cash flows which SGARAs do not impact until they are sold.

It is considered that a timely review of the implementation of AASB 1037 / AAS 35 is necessary in order to determine potential implementation problems associated with IAS 41 before Australian entities are to comply with the equivalent of IAS 41. In addition, Australia has been asked by the International Accounting Standards Board (IASB) to carry out such a review.

**Objectives**

This review aims to identify:

1. difficulties in Australia in implementing AASB 1037 / AAS 35;
2. potential implementation problems with IAS 41; and
3. potential improvements to IAS 41.

**Suggested Approach**

*Scope of Project*

In order to achieve the aims of the review, it is recommended that the work undertaken should involve a comprehensive post implementation review of AASB 1037 / AAS 35 and field testing of IAS 41 in the Australian environment to establish which standard is superior and whether either or both standards require review in the short term and in the longer term.

**AASB Meeting 2-3 September 2003****Agenda paper 6.5.2**

The results from information gathered will determine the way to progress the project, which may involve AASB action in considering implementation issues associated with AASB 1037 / AAS 35 and / or providing feedback to the IASB with suggested improvements to IAS 41.

*Data collection*

It is recommended that information be collected in the first instance through questionnaires. This will provide a preliminary view on the practical difficulties associated with the current requirements of these standards.

It may be necessary to have meetings with entities and individuals who have exhibited strong views through the responses in the questionnaire on the requirements of the standards in order to better understand the effect of both the Australian and International standards on the entity and to consider any recommended solutions which may improve the standards.

Pilot testing of the proposed questionnaire for preparers of accounts was completed by Southcorp Ltd. This assisted in identifying whether the questionnaire adequately addresses potential issues associated with AASB 1037 / AAS 35 and IAS 41.

*Participants in data collection*

In order to establish the effects of the standards on a wide range of affected parties it is recommended that a wide sample of entities and individuals participate in the data collection. The sample should include entities and individuals from 6 major classifications:

1. Preparers of accounts;
2. Auditors;
3. Valuers;
4. Users of accounts;
5. Academics;
6. Representative bodies.

To identify difficulties associated with applying the requirements of the standards for particular industries or types of entities, the sample of Preparers of accounts should be cross-sectioned to differentiate between:

1. Private versus Public;
2. Bearer versus Consumable;
  - 2.1 Different Bearer industries;
  - 2.2 Different Consumable industries;
3. Short-term operations versus long-term operations; and
4. Vertically integrated operations versus stand-alone operations.

**AASB Meeting 2-3 September 2003  
Agenda paper 6.5.2**

*Timing*

It is unlikely that IAS 41 could be revised by Quarter 1, 2004 for mandatory application from 1 January 2005. However, we aim to be well-advanced in the lead up to 2005 for recommending changes to the requirements of IAS 41.

Going forward, the timing of the project will depend on a number of factors including:

- the extent of issues raised by participants;
- the stage at which the Board becomes formally involved; and
- the priority that the IASB gives to a review of IAS 41.

The post implementation review and field testing has been undertaken as an AASB staff initiative, with the collated results from the questionnaires and meetings being considered by the AASB at their September 2003 meeting. This will provide the Board with an opportunity to determine how the information gathered should be utilised and to identify the appropriate course of action.

*Timeline*

A preliminary timeline of this project follows.

2003	March	April	May	June	July	August	Sept	Oct
1. Development and approval of strategy paper	—							
2. Preliminary review / completion of questionnaire by Fosters		—						
3. Update questionnaire / preparation of "non-preparer" questionnaires			—					
4. Questionnaire sent to identified entities and individuals			—					
5. Completed questionnaires received				—	—			
6. Collation of responses						—		
7. Consideration by AASB							—	—
8. Feedback to IASB								—

**Appendices**

The three Appendices that follow contain the questionnaires that were sent to entities and individuals based on their interest in SGARAs.

Appendix 1: Questionnaire for preparers

Appendix 2: Questionnaire for auditors and valuers

Appendix 3: Questionnaire for users (including analysts, credit rating agencies, investors and academics)

AASB SGARAs Questionnaire May 2003 - Preparer

**Appendix 1 – Preparer Questionnaire on AASB 1037 / AAS 35 and IAS 41**  
XX May 2003

«address»

Dear «greeting»

**Accounting for Self-Generating and Regenerating Assets**  
**Post Implementation Review of AASB 1037 / AAS 35 and IAS 41 Convergence Issues**

The Australian Accounting Standards Board (AASB) is seeking your assistance in its review of post implementation issues concerning Australian Accounting Standards AASB 1037 / AAS 35 “Self-Generating and Regenerating Assets” and convergence issues concerning International Accounting Standard IAS 41 “Agriculture”.

To assist with the review, I enclose a copy of a questionnaire that will help the AASB identify post implementation issues for AASB 1037 / AAS 35 and potential implementation issues related to IAS 41. The questionnaire includes specific questions relating to AASB 1037 / AAS 35 and IAS 41. We would appreciate it if you could arrange for the questionnaire to be completed by the entity within your group that has self-generating and regenerating assets to ensure the most significant issues are identified. We understand that you may not yet have considered the impact of IAS 41 on your entity, however we believe it necessary to consider both the Australian and International standards concurrently to identify the likely impact IAS 41 would have on Australian entities when Australia converges with International Accounting Standards in accordance with the strategic direction set by the Financial Reporting Council. We would appreciate all questions being answered as completely as possible.

The AASB will be sending its comments to the International Accounting Standards Board (IASB) on implementation issues identified during the review to provide the IASB with an opportunity to consider these in relation to IAS 41. In addition, the AASB has recently issued an Exposure Draft ED 114 “Request for Comment on IAS 41 Agriculture” as part of the convergence with International Accounting Standards. We have enclosed a copy of the Exposure Draft for your information and would welcome a submission from your entity on the Exposure Draft in order to understand your views.

It should be noted that this questionnaire is designed to identify implementation issues, whilst providing a submission on ED 114 will give you the opportunity to express your views on the accounting requirements for self-generating and regenerating assets.

Any questions on the contents of the document should be directed to the AASB’s Project Manager in charge of this area, Monique Ledden (03 9617 7631 or [mledden@asb.com.au](mailto:mledden@asb.com.au)). In due course, we may seek an opportunity to meet with you to discuss the results of the review.

Your co-operation in this project is greatly valued by the AASB. We would appreciate it if the completed questionnaire could be returned on or before 30 June 2003.

Yours sincerely

Ruth Picker  
Acting Chairman  
\* Enc

AASB SGARAs Questionnaire May 2003 - Preparer

## Description

*Please read this before completing the questionnaire*

### Objectives

The objectives of this questionnaire are to identify issues arising from the implementation of Australian Accounting Standards AASB 1037 / AAS 35 "Self-Generating and Regenerating Assets" and potential convergence issues associated with International Accounting Standard IAS 41 "Agriculture".

The results of the questionnaire will assist the Australian Accounting Standards Board (AASB) to provide feedback to the International Accounting Standards Board (IASB) on any potential issues identified with IAS 41 and any recommendations for improving IAS 41.

### Scope

Questionnaires on the accounting standards are being sent to a wide range of entities and individuals that are affected by, or have an interest in, accounting for self-generating and regenerating assets (SGARAs). Recipients include preparers of accounts, auditors, users of accounts, academics, valuers and representative bodies. The basic questionnaire has been modified for some groups, to tailor the questions based on the group's interest in SGARAs.

### Confidentiality

The identity of individual respondents to this questionnaire will be treated as confidential and will not be disclosed in AASB or IASB papers. The information collected and held by the AASB will not be used for any purpose other than that for which it was collected or disclosed to any other person, agency or body, without the authorisation of the individual concerned unless required or authorised by or under law, or unless the other purpose is reasonably necessary for the enforcement of criminal or other law. The collated results will be available only to the AASB and IASB members and to staff of the AASB and IASB. The name of the entity is requested to enable classification of the response and the name of the individual responsible for answering the questions is requested to facilitate contact if clarification is needed.

### Content of Questionnaire

The questionnaire comprises three parts:

- |         |                                                                                                                                                                                                                                                                                               |                     |
|---------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------|
| PART A: | General questions about your entity.                                                                                                                                                                                                                                                          | <i>20 pages</i>     |
| PART B: | <p>Questions on each type of SGARA, including questions related to AASB 1037 / AAS 35 and IAS 41.</p> <ul style="list-style-type: none"> <li>▪ Please photocopy as many copies of PART B as needed to fill out a separate PART B for each type of SGARA you have listed in PART A.</li> </ul> | <i>17 questions</i> |
| PART C: | General questions on how you think SGARAs should be accounted for.                                                                                                                                                                                                                            | <i>8 questions</i>  |

**Terminology**

AASB SGARAs Questionnaire May 2003 - Preparer

*Agricultural activity:* The management by an enterprise of the biological transformation of biological assets for sale, into agricultural produce, or into additional biological assets. (IAS 41 paragraph 5)

*Agricultural produce:* The harvested product of the entity's biological assets. (IAS 41 paragraph 5)

*Bearer SGARA:* A SGARA where the non-living produce is extracted and the SGARA remains. (AASB 1037 / AAS 35 paragraph 5.5.2)

*Biological asset:* A living animal or plant. (IAS 41 paragraph 5)

*Consumable SGARA:* A SGARA where the extraction of the non-living produce means that the SGARA no longer exists. (AASB 1037 / AAS 35 paragraph 5.5.2)

*Fair value:* The amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. (IAS 41 paragraph 8)

*Net market value:* The amount which could be expected to be received from the disposal of an asset in an active and liquid market after deducting costs expected to be incurred in realising the proceeds of such a disposal. (AASB 1037 / AAS 35 paragraph 10.1)

*Self-Generating and Regenerating Asset (SGARA):* A non-human living asset. (AASB 1037 / AAS 35 paragraph 10.1)

***Please submit the questionnaire online ([www.aasb.com.au](http://www.aasb.com.au)) or return the completed questionnaire by 30 June 2003 to:***

Monique Ledden – Assistant Project Manager

**By email:** [mledden@aaasb.com.au](mailto:mledden@aaasb.com.au)

If emailing, please attach the completed questionnaire as a MS Word document.

**By fax:** (03) 9617 7681

**By post:** Australian Accounting Standards Board  
PO Box 204  
Collins Street West  
Victoria 8007

**Thank you very much for your assistance**

*If you have any questions or would like the questionnaire as a Word doc file, please contact:*

*Monique Ledden, Assistant Project Manager – Australian Accounting Standards Board  
Phone: (03) 9617 7631; Fax (03) 9617 7681; or Email: [mledden@aaasb.com.au](mailto:mledden@aaasb.com.au)*

**APPENDIX 22B: AASB Post Implementation Review****Staff Commentary on PIR Submissions**

AASB Meeting 2-3 September 2003  
 Agenda paper 6.5.3

**Collation of responses received on the AASB Post Implementation  
 Review of AASB 1037/AAS 35 “Self-Generating and Regenerating  
 Assets” and IAS 41 “Agriculture” Convergence Issues**

(Questionnaire distributed and available on AASB website 16 May 2003, comment period closing 30 June 2003)

<b>Classification of Respondents</b>	<b>3</b>
<b><u>Preparers</u></b>	<b>4</b>
<b><u>General</u></b>	<b>4</b>
<i>General information about the preparers</i>	4
<i>General Comments</i>	6
<b><u>Specific Comments</u></b>	<b>9</b>
<b><u>Measurement and Recognition</u></b>	<b>9</b>
Valuation methods for different types of SGARAs	9
SGARAs accounting versus lease accounting	29
<b><u>Scope of Standards</u></b>	<b>30</b>
Exclude from scope of AASB 1037 / AAS 35 and IAS 41	30
Include in scope of AASB 1037 / AAS 35 and IAS 41	32
Special industry / entity features	33
<b><u>Presentation and Disclosure</u></b>	<b>34</b>
Presentation of revenues and expenses from SGARAs	34
Disclosure Requirements	38
<b><u>Auditors and Valuers</u></b>	<b>40</b>
<b><u>General</u></b>	<b>40</b>
<i>General information about the respondent</i>	40
<i>General information about the SGARAs</i>	40
<i>General Comments</i>	41
<b><u>Specific Comments</u></b>	<b>43</b>
<b><u>Measurement and Recognition</u></b>	<b>43</b>
Valuation methods for different types of SGARAs	43
SGARAs accounting versus lease accounting	52
<b><u>Scope of Standards</u></b>	<b>53</b>
Special industry / entity features	53
<b><u>Presentation and Disclosure</u></b>	<b>54</b>
Disclosure Requirements	54

<b>Users</b>	<b>55</b>
<b><u>General</u></b>	<b>55</b>
<i>General information about the respondent</i>	55
<i>General Comments</i>	55
<b><i>Specific Comments</i></b>	<b>57</b>
<i>Measurement and Recognition</i>	57
SGARAs accounting versus lease accounting	57
<i>Scope of Standards</i>	58
Exclude from scope of AASB 1037 / AAS 35 and IAS 41	58
Include in scope of AASB 1037 / AAS 35 and IAS 41	60
Special industry / entity features	60
<i>Presentation and Disclosure</i>	62
Presentation of revenues and expenses from SGARAs	62
Disclosure Requirements	63

The collation deals with responses received on the post implementation review of AASB 1037 / AAS 35 “Self-Generating and Regenerating Assets” and Convergence Issues with IAS 41 conducted by AASB staff. Agenda Paper 6.5.2 outlines the strategy of the post implementation review and contains the pro forma questionnaires that were sent to a number of entities and individuals covering a wide perspective of different interests in SGARAs.

The following structure is used for each specific matter:

- the issue in the questionnaire;
- summary of responses; and
- comments extracted from questionnaire responses.



**Classification of Respondents**

<b>Class</b>	<b>Description</b>	<b>Number of questionnaires sent</b>	<b>Number of responses received</b>
P	Preparers	82	15
AV	Auditors and Valuers	12	7
U	Users	15	3
Total		109	26

## Preparers

### General

#### General information about the preparers

(sorted by ID)

Submission	Private / Public	Industry	Long term / short term operations	Vertically integrated operations
P-1	Private	Distiller and Vintner	Long term	Yes
P-5	Private	Livestock	Short term	No
P-13	Private	Agricultural Products <i>bottom</i>	Mixed	Yes
P-14	Private	Distillers & Vintners	Long term	Yes
P-15	Public	Forest Products	Long term	No
P-16	Private	Brewer & Distiller and Vintner	Long term	Yes
P-27	Private	Forest Products	Long term	No
P-18	Private	Agricultural Products <i>Teas &amp; Wine</i>	Long term	Yes
P-19	Private	Brewer & Distiller and Vintner <i>6 stars</i>	Long term	Yes
P-20	Private	Agricultural Products <i>Seiman</i>	Long term	Yes
P-21	Private	Agricultural Products	Long term	Yes
P-22	Private	Livestock <i>Supine</i>	Short term	No
P-23	Public	Forest Products	Long term	No
P-25				
P-25(1)	Public	Agricultural Products	Short term	No
P-25(2)	Public	Forest Products	Long term	No
P-25(3)	Public	Agricultural Products	Short term	No
P-26	Representative Body	Distiller and Vintner <i>Opinion?</i>		

The majority of the SGARAs that the preparers have, would be within the scope of IAS 41. SGARAs under operating lease (e.g. some grape vines) are outside the scope of IAS 41 and would be required to apply lease accounting.

The majority of preparers do not split the value of the SGARA into current and non-current components. Where the split is done, the current component comprises of the amount expected to be consumed or realised (through sale) in the next 12 months (or operating cycle of the entity).

Four preparers (out of 14 (excludes the representative body)) indicated they use the information about the NMV of SGARAs under AASB 1037 / AAS 35 in making business management decisions. When applying IAS 41, these entities (and one other entity) expect to use the fair value of biological assets in making business decisions.

**General Comments***(sorted by ID)*

Submission	Comment	General comments
P-1	<p>We disagree with having to value these assets (grape vines) at all. It is an estimated derived figure using many variable assumptions, for which there is no active market. Vines are not traded separately only the whole integrated vineyard. We are strongly of the opinion that these bearer SGARAs should be measured on a historic cost basis, which would align the measurement to other integral assets such as land, trellising and irrigation.</p> <p>There is also some confusion in presentation of the Statement of Cash Flows in our industry.</p>	
P-16	<p>Based on our experience, we believe there to be several issues when applying AASB 1037 to the wine industry:</p> <ul style="list-style-type: none"> <li>• there is the potential for significant volatility in SGARA increments / decrements from year to year. Given the non-cash nature of SGARA increments and decrements, we believe that such volatility may result in confusion among users of the financial statements as to the real financial performance of an entity.</li> <li>• the subjective nature of some of the measurement components of the standard requirements complicates the fair valuation of grapes and vines at a point in time. Factors such as yield, market prices and quality of grapes harvested are often uncertain until after the harvest has been completed. As a result, there may be variances in the fair value increment / decrement recognised between reporting periods, where the harvest falls between those reporting periods. Such variances may mislead users attempting to project future financial performance.</li> <li>• due to the lack of overall relevance of the standard to business decisions, we have found that users generally exclude the impact of SGARA accounting when analysing our financial results.</li> <li>• the valuation of our grapes and vines in accordance with AASB 1037 is a lengthy process consuming a significant amount of internal and external resources to provide annual fair value assessments of our grape and vines.</li> </ul> <p>Based on the above points we believe that the application of AASB 1037, to the wine industry, does not provide users with useful information which justifies the cost of obtaining this information.</p> <p>In addition, we have reviewed the proposed IAS 41. Based on this review, we note that all of the above AASB 1037 issues will also exist under IAS 41. Furthermore, we note that IAS 41 requires the following disclosures:</p> <ul style="list-style-type: none"> <li>• the aggregate net fair value increment and decrement of grapes and vines during the period (IAS 41.40)</li> <li>• the net value increment and decrement of vines during the period (IAS 41.50(a))</li> <li>• the net fair value of grapes harvested during the period (IAS 41.48)</li> </ul> <p>These three disclosures will result in the identification of a wine company's vineyard costs, which we believe is commercially sensitive.</p>	

Submission	Comment	General comments
	<p>We also note that vines under exclusive operating leases will no longer be recognised as SGARAs under IAS 41, resulting in a decrease in the carrying value of SGARAs.</p> <p>In conclusion, we believe that the application of both AASB 1037 and IAS 41 have costs that far outweigh the benefits provided to the users of our financial statements.</p>	
P-17	<p>Different approaches by different businesses can produce some inconsistencies in application of AASB 1037 / AAS 35. The valuation of timber and forests (on a current rotation basis) is not reflective of a forestry business which is operated on a perpetual basis.</p>	
P-19	<p>The entity believes there to be no users who either use or understand the net market value information on SGARAs. This is based on experience over the past few years from analysts and fund managers when they are presented with the entity's financial results (an ASX listed company). The entity now discusses its financial results "excluding SGARA".</p>	
P-20	<p>The standard has caused great confusion amongst stakeholders in our company resulting in uncertainty for shareholders, potential investors and financiers. It is difficult to establish reliable measurement in volatile agricultural industries and seems to go against traditional accounting principles.</p> <p>Implementation / measurement of SGARAs on a monthly basis to ensure relevant management accounts is very difficult – it results in a constant reconciliation between pre and post SGARA reporting. The standards (AASB 1037 / AAS 35 and IAS 41) also makes it difficult for financiers and investors to adequately access the performance of our company.</p>	
P-22	<p>In theory, the standard is a good idea as the information contained in the accounts can be interpreted along with available market data. In practice, this exercise is complex and diminishes the value of accounts to the majority of users. For example, analysts have informed us that they do not understand the standard. Their question is why do you book profits before the livestock is sold? Our preferred approach would be to disclose market valuations as a note to the accounts but exclude the market adjustments from the financial statements themselves.</p>	
P-26	<p>The entity believes that wine companies should not be required to prepare financial reports in accordance with the requirements of the agriculture accounting standards (AASB 1037 and IAS 41) for the following reasons:</p> <ul style="list-style-type: none"> <li>• The entity is of the view that the scope adopted and dealt with in SGARA is too broad, and that there are major inherent biological and economic differences between SGARAs i.e. forests, livestock and fruit bearers.</li> <li>• The application of the current agriculture accounting requirements to a wine company creates unrealised profits in relation to SGARA that may not be realised through the sale of wine for up to three years and in some instances four to ten years for fortified wines.</li> <li>• The application of the current agricultural accounting requirements to a wine company makes the financial statements too complex for users (including investment analysts) to interpret and does not improve the users' understanding of the financial results of the wine company.</li> </ul>	

Submission	Comment	General comments
	<ul style="list-style-type: none"> <li>• Investment analysts exclude the agriculture accounting treatment when analysing the financial statements of a wine company, therefore the agriculture accounting requirements are a waste of resources (time and cost) for both the wine companies and the users of the reports i.e.:               <ul style="list-style-type: none"> <li>○ The time of company management in determining, understanding and answering queries on the impact of SGARA; and</li> <li>○ The cost of independent valuers, accountants, auditors, tax specialists etc.</li> </ul> </li> <li>• Wine companies now present and discuss their financial results with investment analysts excluding the agricultural accounting treatment.</li> <li>• The entity is of the view that a vine is a depreciable asset that was adequately dealt with under the previously applicable accounting standards AASB 1010 <i>Accounting for the Revaluation of Non-Current Assets</i> and AASB 1021 <i>Depreciation of Non-Current Assets</i>.</li> </ul>	
	<p>Accordingly, the entity believes that the agricultural accounting standards (AASB 1037 and IAS 41) should be adjusted to exclude the impact of the standards on the wine industry.</p>	

## Specific Comments

### *Measurement and Recognition*

#### Valuation methods for different types of SGARAs

#### **Summary (including general information on valuation methods)**

- Eleven entities (out of 14 (excludes the representative body)) had a comprehensive valuation undertaken for their latest financial year. Two entities (P-14 and P-19) did not have a comprehensive valuation undertaken, and one entity (P-20) did not specify.
- None of the entities have changed any of the underlying assumptions or the measurement method for valuing SGARAs between comprehensive valuations.
- Three entities specified that they adopt short-hand valuation techniques. These consist of:
  - P-16 (Grape Vines) – Short-hand valuations are done for half-year reporting. Short-hand valuations adjust the year-end SGARA values for the expected net fair value of grapes still on the vines;
  - P-19 (Grape Vines, Olive Trees) – Where independent valuations have not been obtained for a particular year, management determined the NMV based on business knowledge of the indicators and assumptions used to value these assets; and
  - P-20 (Apple orchards) – Valuer’s model.
- All entities (that answered the question) identified that they have experienced problems in undertaking a comprehensive valuation of the SGARA in accordance with the AASB 1037 / AAS 35 requirements. The main problems identified were:
  - costs incurred for external consultants (independent valuers), internal labour (management time) and audit costs;
  - differences of opinion on subjective matters between management, valuers and auditors;
  - estimation of yields / assumptions to be used in a valuation model; and
  - little or no information value added to the financial report.
- The majority of entities did not identify additional problems in undertaking a valuation under IAS 41, mainly due to the expectation that the same valuation method as currently applied will be used. However, some entities identified two additional problems under IAS 41 compared with AASB 1037 / AAS 35:
  - the interpretation of IAS 41.21 (specifically whether future growth should be included in the valuation). One entity (P-15) noted that there may be material write-downs if future growth is to be excluded from NPV calculations and that they expected to incur significant compliance costs (above the costs currently incurred to comply with AASB 1037 / AAS 35) relating to this.
  - P-23 identified that there may be a need to change the wood growth modelling process and vary internal costs. The entity will be seeking external advice on this.
- From the 7 entities that have a bearer SGARA attached to land, 6 entities value the bearer SGARA as the difference between the NMV of (a) combined land and bearer SGARA and (b) land. The methods used to estimate the NMV include:

- Independent valuers assess the combined value of land and grapevines. The independent valuation also values the land on a stand alone basis using the estimated value of the land in an undeveloped condition.
- Market values for comparable vineyards are generally available. Value of land and buildings can be separately identified.
- An independent valuation was undertaken on adoption of AASB 1037, where the NMV of the land and bearer SGARA was determined.
- As there is a market for apple orchards, an independent valuer places a value on the total orchard, then deduced the value of the orchard by deducting the value of land and buildings.
- Asset values deducted from cumulative cash flows to determine tree value based on current valuation and adjusted annually to account for capital expenditure, depreciation and utilised acreage.
- The main valuation methods used for the different types of SGARAs are:
  - Grape vines – Net present value (4 out of 5 entities);
  - Livestock – Net market value of the asset in an active and liquid market (all 4 entities);
  - Forests / Plantations – Net present value (7 out of 8 entities);
  - Orchards / Trees – Net present value (4 out of 7 entities);
  - Cotton<sup>1</sup> – Mixed valuation methods for the one entity;
  - Fruits / Nuts<sup>1</sup> - Net market value of the asset in an active and liquid market (2 out of 3 entities);
- Based on the 14 preparers (excludes the representative body):
  - 10 entities believed that their SGARA(s) can be valued reliably on a consistent basis at each reporting using the valuation methods that they apply;
  - 1 entity (P-13) had mixed views believing their grape vine valuations are reliable, however their valuation of cotton is possibly not reliable;
  - 2 entities did not believe that reliable valuations are possible; and
  - 1 entity (P-20) did not provide comment.

---

<sup>1</sup> We believe that the information provided relates to produce (inventory) from the SGARAs



**Comments extracted from submissions**  
(sorted by position then ID)

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(c)(i), (ii))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
<b>GRAPE VINES</b>								
P-1 (Mainly owned, but some leased under operating lease)	Net present value (d)	Risk in Discount rate Discount rate – Asset specific, After Tax 10 year cash flow projection. Future growth – model allows for a yield and grade factor to be incorporated into the calculation.	Net present value (e)	Risk in Discount rate Discount rate – Asset specific 10 year cash flow projection. Future growth – model allows for a yield and grade factor to be incorporated into the calculation.	No	No	Yes	Yes
P-13 (Owned)	Net present value (d)	Risk in Discount rate and cash flows Discount rate –	Net present value (e)	Risk in Discount rate and cash flows Discount rate –	No	No	Yes	Yes

<sup>2</sup> The letter beside the valuation method represents the valuation method identified in Question B4 of the Preparer Questionnaire (refer to SGARAs Strategy Paper).

<sup>3</sup> The letter beside the valuation method represents the valuation method identified in Question B5 of the Preparer Questionnaire (refer to SGARAs Strategy Paper).

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuations (B2h, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
P-14	Net present value (d)	Industry benchmarks, After Tax 20 year cash flow projection. Future growth – Vines are now mature, do not anticipate future growth. Risks in cash flow – Yield assumptions, and conservative on sell price.	Net present value (e)	Industry benchmarks 20 year cash flow projection. Future growth – Vines are now mature, do not anticipate future growth. Risks in cash flow – Yield assumptions, and conservative on sell price.	No	No	assumptions (major variables are discount rate, yield and life of the vine)	assumptions (major variables are discount rate, yield and life of the vine)
	Net present value (d)		Net present value (e)		No	No	assumptions (major variables are discount rate, yield and life of the vine)	assumptions (major variables are discount rate, yield and life of the vine)

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
P-16 (Grape vines (owned and under operating lease) and grapes)	Net market value of related assets (c)	Independent valuations were obtained for all owned vineyards, based on the estimated net selling price. The value of the grapevines was determined by deducting the value of all	Market prices for similar or related assets (c)	Independent valuations will be obtained for all owned vineyards, based on the estimated net selling price. The value of the grapevines will be determined by deducting the	Yes - Grape vines under operating lease will be subject to lease accounting (IAS 41).	Yes - Grape vines under operating lease will be subject to lease accounting (IAS 41).	Yes External consultants will provide valuation.	Yes External consultants will provide valuation.
							sensical to try and split the value of the land and the vines as they are intrinsically linked. Consequently we rely on DCF techniques as prescribed in the standard which are of questionable validity.	sensical to try and split the value of the land and the vines as they are intrinsically linked. Consequently we rely on DCF techniques as prescribed in the standard which are of questionable validity.

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (BS) <sup>3</sup>	Information on IAS 41 valuation (BS)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – IAS 41 (B2(d)(i), (ii))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))
P-19	Net present value (d)	Risk in Discount rate and cash flows Discount rate – Industry benchmarks adjusted for any business specific issues, Pre Tax 3 – 5 year cash flow projection. Future growth – The business looks at future growth of wine, not vine or grapes. The SGARA valuation increment or decrement is	Net present value (e)	Risk in Discount rate and cash flows Discount rate – Industry benchmarks adjusted for any business specific issues 3 – 5 year cash flow projection. Future growth – The business looks at future growth of wine, not vine or grapes. The SGARA valuation increment or decrement is non-cash	No	No	Possible Not A NMV for vines can be determined, however it is not considered to be a reliable measure to financially account for this asset on this basis.	Possible Not A NMV for vines can be determined, however it is not considered to be a reliable measure to financially account for this asset on this basis.
		non-SGARA assets from the value of the total vineyard.		value of all non-SGARA assets from the value of the total vineyard.				

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
		non-cash therefore no cash impact. Risks in cash flow – Vintage – being surplus or shortage of grapes from a particular harvest period. Risk is mitigated by having vineyards in different countries and appellations.		therefore no cash impact. Risks in cash flow – Vintage – being surplus or shortage of grapes from a particular harvest period. Risk is mitigated by having vineyards in different countries and appellations.				

**LIVESTOCK**

P-5 (Breeding and non-breeding cattle, sheep)	Net market value of the asset in an active and liquid market (a)	Domestic and export beef market and also an export market for live cattle.	Net market value of the asset in an active and liquid market (a)	Domestic and export beef market and also an export market for live cattle.	No	No	Yes	Yes
P-20 (Salmon)	Cost (e) (for fish <2kg) Net market		Cost (f) (for fish <2kg) Market value		No		Yes A ready, established market exists.	

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuations methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
	price for similar or related assets (b) (for fish >2kg)		for similar or related assets (b) (for fish >2kg)					
	Due to the difficulty in coming up with a reliable market price, we are currently proposing to revert to cost for all salmon.		Due to the difficulty in coming up with a reliable market price, we are currently proposing to revert to cost for all salmon.					
P-22 (Swine)	Net market value of the asset in an active and liquid market (a)	Sows futures and current prices.	Market price of the asset in an active market (a)	Sows futures and current prices.	No	No	Yes	Yes
P-25(1) and P-25(2) (Livestock, cattle)	Net market value of the asset in an active and liquid market (a)	Livestock saleyards Either sales close to year end or market prices at balance date	Net market value of the asset in an active and liquid market (a)	Livestock saleyards Either sales close to year end or market prices at balance date	No	No	Yes	Yes P-25(1) is currently using active and liquid markets to determine NMV.

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
		within the industry.		within the industry.			
					NMV.		
							P-25(3) – An estimate of cattle numbers is provided at year end. Prices will be taken from either sales prior to year end, or if no sales are made close enough to year end, market prices from within industry are taken.
							P-25(3) – An estimate of cattle numbers is provided at year end. Prices will be taken from either sales prior to year end, or if no sales are made close enough to year end, market prices from within industry will be taken.

**FORESTS / PLANTATIONS**

P-15 (Standing Timber made up of native forest standing timber, Standing sandalwood and Reforestation program)	Net present value (d)	Risk in Discount rate	Discount rate – WACC, Pre Tax	50 year cash flow	Net present value (e)	Risk in Discount rate	Discount rate – WACC	50 year cash flow	projection, 30	No	Yes	
										This will depend on the interpretation of IAS 41.21. The wording at present would lead to a decrease in	NPV assumptions are applied consistently.	NPV assumptions are expected to be applied consistently (subject to T.C. 41.21)

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>3</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
P-15 (Plantation standing timber)	Net present value (d)	Risk in Discount rate – WACC, Pre Tax 30 year cash flow projection Future growth – Growth is an integral part of the valuation.	Net present value (e) Market price of the asset in an active market (a)	Risk in Discount rate – WACC 30 year cash flow projection Future growth – Growth is an integral part of the valuation. Cash flow	Under IAS 41 the market price will be considered if future growth is excluded from the SGARA (Application of IAS 41.21).	Under IAS 41 the market price will be considered if future growth is excluded from the SGARA (Application of IAS 41.21).	Net present value assumptions are applied consistently.	Net present value assumptions are expected to be applied consistently (subject to IAS 41.21 interpretation).
	Valuation method – AASB 1037 / AAS 35 (B4) <sup>3</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
		projection, 30 years for reforestation program Future growth – Growth is an integral part of the valuation. Cash flow calculations are based on assumptions relating to the SGARA maturing into the future.		years for reforestation program Future growth – Growth is an integral part of the valuation. Cash flow calculations are based on assumptions relating to the SGARA maturing into the future.		values as IAS 41.21 appears to exclude future growth.		IAS 41.21 interpretation).



Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
		Cash flow calculations are based on assumptions relating to the SGARA maturing into the future.		calculations are based on assumptions relating to the SGARA maturing into the future. Market price will be considered if future growth is excluded from the SGARA (IAS 41.21).				
P-17 (Forestry, timber)	Net present value (d)	Risk in Discount rate -- Discount rate -- Based on comparable sales / valuation, Pre Tax	Net present value (e)	Risk in Discount rate -- Discount rate -- Based on comparable sales / valuation	No	No	Yes	Yes
		60 year perpetual cash flow projection, however only		30 year cash flow projection				
				Future growth – Yields built into forestry				

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
		current crop projected for SGARA purposes (30 years).		date on which valuation based.				
P-23 (100% owned native forest eucalypts)	Net present value (d)	Risk in combination of discount rate and cash flow Discount rate – WACC, Pre Tax 90 year cash flow projection Future growth – mean annual increments Cash flow risks – future prices	Net present value (e)	Risk in combination of discount rate and cash flow Discount rate – WACC 90 year cash flow projection Future growth – dependent on IAS 41.21 Cash flow risks – future prices	No	Value expected to be different due to guidance in IAS 41.21.	Yes	Yes
P-23 (100% owned softwood plantations, 100% owned hardwood plantations)	Net present value (d)	Risk in combination of discount rate and cash flow Discount rate – Implied market discount rate,	Net present value (e)	Risk in combination of discount rate and cash flow Discount rate – Implied market discount rate	No	Value expected to be different due to guidance in IAS 41.21.	Yes	Yes

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
P-23 (Joint Venture softwood plantations)		Pre Tax 30 and 26 year cash flow projection		30 and 26 year cash flow projection				
		Future growth – mean annual increments Cash flow risks – future prices		Future growth – dependent on IAS 41.21 Cash flow risks – future prices				
	Net present value (d)	Risk in combination of discount rate and cash flow Discount rate – Mean implied discount rate, for market sales that have occurred over the last 5 – 6 years, Pre Tax 28 year cash flow projection Future growth – mean annual increments	Net present value (e)	Risk in combination of discount rate and cash flow Discount rate – Mean implied discount rate, for market sales that have occurred over the last 5 – 6 years 28 year cash flow projection Future growth – dependent on IAS 41.21	No	Yes	Yes	Yes
						Value expected to be different due to guidance in IAS 41.21.		

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – IAS 41 (B2(d)(i), (ii))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))
		Cash flow risks – future prices						
P-23 (Joint Venture hardwood plantations)	Cost (e)	Little biological change.	Cost (f)	Little biological change.	No	No	Yes	Yes
P-25(2) (Plantation timber)	Net present value (d)	Risk in discount rate – WACC (set with reference to industry benchmarks), After Tax	Net present value (e)	Risk in discount rate – WACC (set with reference to industry benchmarks)	No	No	Yes	Yes
		0 - 50 years (until harvest maturity of all existing standards) cash flow projection		0 - 50 years (until harvest maturity of all existing standards) cash flow projection			Calculation of NPV will be reliable if the valuation assumptions are applied consistently across reporting periods.	Calculation of NPV is reliable and consistent across reporting periods.
		Future growth – biological growth and yield models		Future growth – biological growth and yield models				

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
<b>ORCHARDS / TREES</b>								
P-18 (Trees and vines)	Net present value (d)	Risk in combination of discount rate and cash flows Discount rate – Industry benchmark, Pre Tax	Net present value (e)	Risk in combination of discount rate and cash flows Discount rate – Industry benchmark 33 year cash flow projection	No	No	Yes DCF methodology	Yes DCF methodology
		Future growth – Although we have immature and mature orchards, the model we use accounts for only mature trees.		Future growth – Although we have immature and mature orchards, the model we use accounts for only mature trees.				
		Risks in Cash flow – crop maturity levels, agricultural risk.		Risks in Cash flow – crop maturity levels, agricultural risk.				

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
P-19 (Olive trees)	Net present value (d)	Risk in Discount rate and cash flows Discount rate – Pre Tax 3 year cash flow projection. Future growth – Nil. Not a core business or material to forecast growth.	Net present value (e)	Risk in Discount rate and cash flows 3 year cash flow projection. Future growth – Nil. Not a core business or material to forecast growth.	No	No	Possibly Not A NMV for vines can be determined, however it is not considered to be a reliable measure to financially account for this asset on this basis.	Possibly Not A NMV for vines can be determined, however it is not considered to be a reliable measure to financially account for this asset on this basis.
P-20 (Apple orchards)	Net market value for similar or related assets (b)	As there is a market for apple orchards, we contracted a value to place a value on the total orchard, then deducted the value of the orchard by deducting the value of land and buildings.	Market prices for similar or related assets (c)	As there is a market for apple orchards, we contracted a value to place a value on the total orchard, then deducted the value of the orchard by deducting the value of land and buildings.	No	No	As there is a market for apple orchards, we contracted a value to place a value on the total orchard, then deducted the value of the orchard by deducting the value of land and buildings.	As there is a market for apple orchards, we contracted a value to place a value on the total orchard, then deducted the value of the orchard by deducting the value of land and buildings.

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
P-20 (Walnut orchards)	Net present value (d)		Net present value (e)	No				
P-20 (Cherry orchards)	Cost (e)	We only purchased the cherry orchard recently and do not generate income from it. We used our purchase price as the most reliable measure of NMV.						
P-20 (Walnut trees – consumable SGARA)	Net market value of the asset in an active and liquid market (a)	Stock separated into the expected final markets and use pricing based on known prices in those markets.	Market price of the asset in an active market (a)	Stock separated into the expected final markets and use pricing based on known prices in those markets.				
P-21 (Almond trees)	Net present value (d)	Risk in Discount rate – Industry	Net present value (e)	Risk in Discount rate – Industry	No	No	Yes	Yes

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>a</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>b</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
P-13	Net market value of the asset in an active and liquid market (a) Cost (e) A basis for determining net market value other than one explicitly listed (f)	(a) Cotton futures to determine price. Most cotton is sold years in advance. (e) Cost is used to build up the valuation. This is easily obtained and readily estimated.	Market price of the asset in an active and liquid market (a) Cost (f)	(a) Cotton futures to determine price. Most cotton is sold years in advance. (f) Cost is used to build up the valuation. This is easily obtained and readily estimated.	Only difference is that a basis is expected to be used.	No	Possibly Not The three major variables are cotton prices for unsold cotton, anticipated yields and back production. We can only rely on history.	Possibly Not The three major variables are cotton prices for unsold cotton, anticipated yields and back production. We can only rely on history.
<b>COTTON</b>								
P-13	Valuation method – AASB 1037 / AAS 35 (B4) <sup>a</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>b</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
	benchmarks, Pre Tax 30 year cash flow projection. Future growth – Through crop yields anticipated during life cycle of asset.	benchmarks, 30 year cash flow projection. Future growth – Through crop yields anticipated during life cycle of asset.	IAS 41 (B5) <sup>b</sup>	IAS 41 valuation (B5)	B4, B5)	(B2(b))	(B2(c)(i), (ii))	(B2(d)(i), (ii))



Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(e)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
P-13 (Tree fruits)		Information on AASB 1037 / AAS 35 valuation (B4)  (f) History is used to predict yields and production output. This is a key area in determining the final valuation.	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)  Risk in Discount rate and cash flows Discount rate – industry benchmarks 20 year cash flow projection. Future growth – Trees are now mature, do not anticipate future growth. Risks in cash flow – Yield assumptions.	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(e)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
<b>FRUITS / NUTS</b>								
P-13 (Tree fruits)	Net present value (d)	Risk in Discount rate and cash flows Discount rate – industry benchmarks, After tax 20 year cash flow projection. Future growth – Trees are now mature, do not anticipate future growth. Risks in cash flow – Yield	Net present value (e)	Risk in Discount rate and cash flows Discount rate – industry benchmarks 20 year cash flow projection. Future growth – Trees are now mature, do not anticipate future growth. Risks in cash flow – Yield	No	No	Yes Value will be reliable as long as we are consistent with the assumptions (major variables are discount rate, yield and life of the tree).	Yes Value will be reliable as long as we are consistent with the assumptions (major variables are discount rate, yield and life of the tree).

Submission	Valuation method – AASB 1037 / AAS 35 (B4) <sup>2</sup>	Information on AASB 1037 / AAS 35 valuation (B4)	Valuation method – IAS 41 (B5) <sup>3</sup>	Information on IAS 41 valuation (B5)	Difference between valuation methods (B2b, B4, B5)	Difference between AASB 1037 and IAS 41 value (B2(b))	Reliable valuation – AASB 1037 (B2(c)(i), (ii))	Reliable valuation – IAS 41 (B2(d)(i), (ii))
		assumptions, and conservative on sell price.		and conservative on sell price.				
P-20 (Apples, onions, carrots, walnuts)	Net market value of the asset in an active and liquid market (a)	Current season prices.	Market price of the asset in an active market (a)	Current season prices.	No	No	Yes	Yes
P-21 (Almond growing crops, almond stocks harvested)	Net market value of the asset in an active and liquid market (a)	Prices from established international almond markets.	Market price of the asset in an active market (a)	Prices from established international almond markets.	No	No	Yes	Yes

SGARAs accounting versus lease accounting**Summary**

Entities with a SGARA held under an exclusive right were asked whether “SGARAs accounting” contains more useful information than “lease accounting”. Mixed responses were received with 3 entities believing SGARAs accounting is more useful and 2 entities believing lease accounting is more useful.

**Comments extracted from submissions**

*(sorted by position then ID)*

<b>Submission</b>	<b>Comment</b>	<i>SGARAs vs Lease accounting</i>
<b>SGARAs accounting</b>		
P-15 (Forest)	Very little of the land on which the entity’s SGARAs resides is vested in the Commission. Exclusive rights are granted through the entity’s enabling legislation, the <i>Forest Products Act 2000</i> . Disclosure requirements per AASB 1037 / IAS 41 are more appropriate than disclosure under finance lease accounting requirements.	
P-16 (Grape vines)	Given the value of specific grapes from specific regions, exclusive rights over the use of these grapes represents significant value to our business. Therefore, these leases should be capitalised as currently allowed under AASB 1037.	
P-17 (Lease of land on which timber owned)	Value is in the trees. Land is not of any real value to forestry business.	
<b>Lease accounting</b>		
P-1 (Grape vines)	The ability to access the grapes is through the lease payment, just like any other lease (e.g. motor vehicle) and should be treated the same way. Attributing an asset value to operating lease arrangements is not appropriate.	
P-19 (Grape vines)	(No specific comment)	

*Scope of Standards*Exclude from scope of AASB 1037 / AAS 35 and IAS 41Summary

Seven entities indicated that they believed that harvested grapes, grape vines, bearer SGARAs and livestock traded on an open market (that are currently within the scope of AASB 1037 / AAS 35) should be excluded from the scope because the cost of AASB 1037 / AAS 35 accounting outweighs the benefits. Another 7 entities believed that no SGARAs should be excluded from the scope of AASB 1037 / AAS 35. One entity did not comment.

Two entities indicating that SGARAs should be excluded from the scope of AASB 1037 / AAS 35 believed that no SGARAs (biological assets) should be excluded from the scope of IAS 41.

Comments extracted from submissions*(sorted by position then ID)*

<b>Submission</b>	<b>Comment</b>	<b>Exclude from scope</b>
P-1	<p>Harvested grapes, vines, bearer SGARAs</p> <p>There are no benefits and market analysts exclude SGARA values and unrealised profits from their wine company assessments. It is the cause of an immense amount of confusion. Generally no wine company uses SGARA in managing their company. We contend that all bearer SGARAs should be excluded for the same reasons, as well as:</p> <ul style="list-style-type: none"> <li>• it does not make sense to measure the bearer SGARA at an estimated fair value while all other asset classes, including assets integrated with the bearer SGARA (e.g. land, plant and equipment) can be measured on a historical cost basis</li> <li>• if the produce is sold, the sale will be recognised at fair value anyway. If the produce becomes a raw material for further processing / manufacturing, it is more appropriate to measure it on a historical cost basis like all other raw materials</li> <li>• bearer SGARAs are similar in nature to plant and equipment</li> <li>• many bearer SGARAs (e.g. grape vines) are not traded as stand-alone assets, which inhibits the reliability of measurement</li> <li>• valuations of bearer SGARAs are highly subjective and can lack comparability between entities.</li> </ul> <p>We disagree with having to value these assets at all. It is an estimated derived figure using many variable assumptions, for which there is no active market. Vines are not traded separately only the whole integrated vineyard.</p> <p>We are strongly of the opinion that these bearer SGARAs should be measured on a historical cost basis, which would align the measurement basis to the other integral assets such as land, trellising and irrigation.</p>	
P-16	Grapevines and grapes should be excluded from the scope of AASB 1037. (Also see General Comments.)	
P-18 (Applicable to scope of only AASB 1037/ AAS 35)	We were not in favour of AASB 1037 including bearer SGARAs as the information supplied to investors / shareholders does not provide any further knowledge of the business and its performance.	

<b>Submission</b>	<b>Comment</b>	<i>Exclude from scope</i>
P-19	The entity would like to see the IAS 41 Agriculture requirements amended to exclude wine businesses from adopting the requirements of fair value accounting for vines, on the basis that there are no users of the fair value information. Experience has shown that analysts and investors are more interested in the market value of the wine that is produced from the grapes from the vine, and the market value of the olive oil that is produced from the olives born by the trees. (Also see General Comments.)	
P-20 (Applicable to scope of only AASB 1037/AAS 35)	For the Group, the cost in terms of understandability has outweighed the benefit.	
P-22	Livestock that is traded on an open market. The effect of the standard is to recognise profit before it is actually realised where market prices less selling costs are greater than cost. This "profit" may never be realised. The cost of disclosing the information outweighs the benefit: <ol style="list-style-type: none"> <li>1. valuations can be misleading as agricultural markets are volatile and can be subject to major unpredictable changes e.g. due to outbreaks of disease.</li> <li>2. the treatment is inconsistent with valuation of our other trading stock e.g. stock feed.</li> <li>3. it is confusing as prices used to value stocks at year end will be different from when the actual livestock is sold and again different from current prices when the user of the accounts analyses the results.</li> </ol>	
P-26	The entity believes that wine companies should not be required to prepare financial reports in accordance with the agriculture accounting standards (AASB 1037 and IAS 41). (Also see General Comments.)	

Include in scope of AASB 1037 / AAS 35 and IAS 41

**Summary**

Thirteen entities believed that all SGARAs should remain included in the scope of AASB 1037 / AAS 35. Two entities did not comment. The same belief on including SGARAs (biological assets) in the scope of IAS 41 was held by all but two entities.

**Comments extracted from submissions**

*(sorted by position then ID)*

<b>Submission</b>	<b>Comment</b>	<b>Include in scope</b>
P-15	Exclusive rights e.g. those obtained through finance leases	
P-16	Given the value of specific grapes from specific regions, exclusive rights over the use of these grapes represent significant value to our business. Therefore, these leases should be capitalised as currently allowed under AASB 1037.	

Special industry / entity features**Summary**

Seven entities indicated that there are special features of their entity or industry where the cost outweighs the benefits of SGARAs accounting in accordance with AASB 1037 / AAS 35 and IAS 41. The main special features identified were:

- Wine companies (mainly due wine companies running a vertically integrated operation);
- Annual crops / products with short life cycles and companies with volatile pricing; and
- Small companies.

It should be noted that 5 of the entities that identified a special feature also identified SGARAs (biological assets) of a similar nature that they believed should be excluded from the scope of AASB 1037 / AAS 35 and IAS 41.

Another 7 entities believed that their entity or industry did not have any special features where the cost outweighs the benefits of SGARAs accounting in accordance with AASB 1037 / AAS 35 and IAS 41. One entity did not comment.

**Comments extracted from submissions**

*(sorted by position then ID)*

<b>Submission</b>	<b>Comment</b>	<b>Special industry / entity features</b>
P-1	We believe that grape vines / grapes specifically and bearer SGARAs and their produce generally should be excluded.	
P-13	Capturing accurate and meaningful information at the various stages of production is not easy at the shop floor level. This becomes even more of an issue with multiple crop years running.	
P-16	We believe that the application of AASB 1037, to the wine industry, does not provide users with useful information which justifies the cost of obtaining this information. (Refer to general comments.) We believe that the costs required to apply the SGARA / Agriculture standards far outweighs the benefits these standards provide to the users.	
P-17	Size of assets to small companies.	
P-19	The entity has a wine business, not a vine or grape business. Being a brand business, but running a vertically integrated operation means that the entity is exposed to accounting for its vines and grapes in accordance with the SGARA requirements, however there are no users of this information. The users of the entity's financial report require information on the value of wine sold – which is when cash is generated by the business.	
P-20	The industries / products have very short life cycles and very volatile pricing making reliable measurement extremely difficult.	
P-26	The entity believes that wine companies should not be required to prepare financial reports in accordance with the requirements of the agriculture accounting standards (AASB 1037 and IAS 41). (Also see General Comments).	

***Presentation and Disclosure***

**Presentation of revenues and expenses from SGARAs**

Preparers were asked:

- (a) How does your entity present revenues and expenses from SGARAs in the Statement of Financial Performance and the notes to the financial statements?
- (b) In the absence of standard requirements to present revenues and expenses from SGARAs, does your entity consider that its presentation method is the most useful method for users of the financial statements?

**Summary**

Entities provided mixed responses on whether their current presentation of revenues and expenses from SGARAs provides the most useful information for users.

**Comments extracted from submissions**

*(sorted by position then ID)*

<b>Submission</b>	<b>Comment</b>	<b>Presentation of revenues and expenses from SGARAs</b>
	<b>METHOD</b>	<b>REASON FOR USEFULNESS / NON-USEFULNESS TO USERS</b>
<b>PRESENTATION METHOD USEFUL FOR USERS</b>		
P-5	Separate disclosure in notes to the financial statements.	No comment.
P-15	<p>“Total revenue from ordinary activities” includes revenues only where the risks and rewards of ownership have passed and for movements in the net market value of harvested timber.</p> <p>Valuation adjustments relating to the net market value of standing timber are reflected as a separate line item and, although monitored quarterly for management accounting purposes, only brought to account annually for financial reporting purposes. This line item remains within the “profit and loss from ordinary activities” section of the statement of financial performance.</p>	<p>In our opinion our presentation represents a practical solution to AASB 1037’s requirement to bring revenue to account as the SGARA is harvested, and avoids duplication in the recognition of revenue.</p> <p>However, we would prefer the valuation adjustments that bring our Standing Timber valuations in line with net market value to be reflected after the “profit and loss from ordinary activities” section of the statement of financial performance.</p>
P-16	Revenues and expenses relating to grapevines and grapes are separately disclosed in our SGARA note. These amounts are included in “Other revenue” and “Other expenses” on the face of our Statement of Financial Performance.	Separate disclosure of SGARA revenues and expenses, in the notes to the financial statements, is sufficient for the users to make any adjustments to back out the SGARA impact on the statement of financial performance.
P-18	Revenues and expenses are recognised as a net change in the statement of financial performance.	If the revenues and expenses were too detailed, it would confuse users and clutter the financial statements.



Submission	Comment	Presentation of revenues and expenses from SGARAs
	METHOD	REASON FOR USEFULNESS / NON-USEFULNESS TO USERS
P-23	Forest net market value increment / decrement is shown separately on the face of the statement from operating revenue and expenses.	(No comment)
P-25(2)	Changes in NMV presented as revenue with a note elaborating on realised / unrealised elements of revenues. An unrealised revenue reserve has been created.	The concept is difficult and different from most other industries. We have endeavoured to present it as clearly as possible.
P-25(3)	Revenues are presented as increases in the market value of the SGARA. All expenses, other than those included in the calculation of net market value, are shown separately as a single line item in the notes to the financial statements.	Presentation provides all relevant information for users of the costs associated with those assets.

**PRESENTATION METHOD IS NOT USEFUL FOR USERS**

P-1	<ul style="list-style-type: none"> <li>Revenues are recognised on harvesting the grapes from the grape vines</li> <li>Revenues / expenses are recognised for the net increment / decrement in the value of the grape vines</li> <li>Vineyard operating expenses are classified as other expenses</li> <li>Sales revenues are recognised when the wine is sold, or when applicable when grapes (immaterial to company) are sold</li> <li>No adjustments are made to eliminate double counting</li> </ul>	It is confusing to all users and even those within the company. If we have to continue with SGARAs it would be better to present a "pre-SGARA" profit and loss similar to what we currently present to the analysts, and then aggregate all SGARA amounts in a single line with separate note disclosure to break out the components. The preferred option would however have to have bearer SGARAs and their produce excluded from the SGARA requirements.
P-13	<ul style="list-style-type: none"> <li>Prior crops actual sales are netted off by prior year SGARA entries</li> <li>Current year estimates production is used to calculate value of inventory to harvest stage plus profit to stage. Cotton for example has further value and process which haven't started yet.</li> </ul>	Users have no idea as to how the revenue has been calculated. A breakdown of the various stages of production are never disclosed.
P-17	Sales revenue	A clearer presentation is needed.

<b>Submission</b>	<b>Comment</b>	<i>Presentation of revenues and expenses from SGARAs</i>
	<b>METHOD</b>	<b>REASON FOR USEFULNESS / NON-USEFULNESS TO USERS</b>
	Market valuation movement.	Information disclosed is not all that meaningful.
P-19	<p>The current net market value increment in SGARA, net of the reversal of prior period valuation increments (reversed when wine is sold), is disclosed as revenue. Expenses include vineyard operating expenses incurred in the current period (that were previously capitalised into wine inventory), net of a reversal to cost of sales for the amount of prior period vineyard operating expenses that have continued to be included in the inventory costing system.</p> <p>The entity is aware that certain other Australian wine companies net SGARA related expenses against the revenue line. Audit firms either accept this inconsistent reporting treatment or the technical requirements of SGARA are so difficult that auditor firms cannot agree on a consistent treatment.</p>	<p>The accounting treatment for SGARA in a wine business is too technical and difficult for an average user of a financial report to understand. This is demonstrated by the inconsistent accounting treatments accepted by audit firms.</p>
P-20	Sales of SGARAs are included in sales revenue and cost of sales with the increment in value disclosed separately. This was previously done in the Statement of Financial Performance but will be disclosed in the notes in the future.	Shareholders mistakenly believe that all of our SGARA income is unrealised – we are now reviewing whether to disclose realised versus unrealised.
P-22	We note the effect on revenue and disclose the accounting policy applied.	<p>In theory, the standard is a good idea as the information contained in the accounts can be interpreted along with available market data. In practice, this exercise is complex and diminishes the value of accounts to the majority of users. For example, analysts have informed us that they do not understand the standard. Their question is why do you book profits before the livestock is sold? Our preferred approach would be to disclose market valuations as a note to the accounts but exclude the market adjustments from the financial statements themselves.</p>
P-25(1)	Net increments / decrements in valuation of SGARAs is included in	Given that the net increment in valuation is unrealised revenues,

Submission	Comment	<i>Presentation of revenues and expenses from SGARAs</i>
	<b>METHOD</b>	<b>REASON FOR USEFULNESS / NON-USEFULNESS TO USERS</b>
	the statement of financial performance.	users of the financial statements may believe that there is more revenue available than there is.

Disclosure Requirements

**Summary**

Entities provided mixed responses on the disclosures required by AASB 1037 / AAS 35. Eight entities did not have any specific issues with the requirements (however one entity noted that they are generally against disclosing sensitive information), 5 entities had specific issues with the disclosure requirements and 2 entities did not comment. The specific issues with the disclosure requirements consisted of:

- difficulty in obtaining the information;
- ambiguity in the disclosure requirements;
- disclosure of commercially sensitive information; and
- other reasons for example the lack of users of the information and the information misleading shareholders by not differentiating between realised and unrealised income.

The majority of entities had the same views on the disclosure requirements in IAS 41. However, it should be noted that 1 entity that did not have any specific issues with AASB 1037 / AAS 35 disclosure requirements, but believes there are a number of commercially sensitive disclosure requirements in IAS 41.

**Comments extracted from submissions**

*(sorted by position then ID)*

Submission	Comment		Disclosure Requirements
	AASB 1037 / AAS 35 Disclosures	IAS 41 Disclosures	
P-1	No specific issues. However, we are generally against disclosing any commercially sensitive information.	No specific issues. However, we are generally against disclosing any commercially sensitive information.	
P-5	No specific issues.	No specific issues.	
P-13	Yes – difficulty in obtaining the information. Yes – ambiguity in the disclosure requirements Yes – disclosure of commercially sensitive information. The process is long and tedious and can rely on interpretation and best estimates. Our preference would be to not disclose as detailed profit numbers.	Yes – difficulty in obtaining the information. Yes – ambiguity in the disclosure requirements Yes – disclosure of commercially sensitive information. The process is long and tedious and can rely on interpretation and best estimates. Our preference would be to not disclose as detailed profit numbers.	
P-15	No specific issues.	No specific issues.	
P-16	No specific issues.	Yes – disclosure of commercially sensitive information.  IAS 41 requires separate disclosure of the following: (a) the aggregate fair value increment and decrement for grapevines (IAS 41.40), (b) the net increment or decrement relating to grapevines only (IAS 41.50), and	

Submission	Comment	Disclosure Requirements	
		AASB 1037 / AAS 35 Disclosures	IAS 41 Disclosures
			(c) net fair value of grapes harvested during the period (IAS 41.48). Using these disclosures our vineyard costs could be identified by deducting the increment / decrement relating to grapes from the fair value of those grapes.
P-17	Yes – difficulty in obtaining the information Yes – ambiguity in the disclosure requirements Yes – disclosure of commercially sensitive information Yes – other	Yes – difficulty in obtaining the information Yes – ambiguity in the disclosure requirements Yes – disclosure of commercially sensitive information	
P-18	No specific issues.	No specific issues.	
P-19	Yes – other. There appears to be no users of this information.	Yes – other. There appears to be no users of this information.	
P-20	Yes – other Shareholders mistakenly believe that all of our SGARA income is unrealised – we are now reviewing whether to disclose realised versus unrealised.	Yes – other Shareholders mistakenly believe that all of our SGARA income is unrealised – we are now reviewing whether to disclose realised versus unrealised.	
P-21	No specific issues.	No specific issues.	
P-22	Yes - other Our preferred approach would be to disclose market valuations as a note to the accounts but exclude the market adjustments from the financial statements themselves.	Yes - other Our preferred approach would be to disclose market valuations as a note to the accounts but exclude the market adjustments from the financial statements themselves.	
P-23	No specific issues.	No specific issues.	
P-25	No specific issues.	No specific issues.	

## Auditors and Valuers

### General

#### *General information about the respondent*

	Type of Response		Main Activities in SGARAs			
	Firm wide	Personal	Audit / Review <sup>4</sup>	Independent valuation <sup>5</sup>	Valuation for financial reporting <sup>6</sup>	Other
AV-4	✓			✓	✓	
AV-8		✓	✓			✓
AV-10	✓		✓			
AV-11		✓	✓			✓
AV-12		✓	✓			✓
AV-24	✓		✓			

#### *General information about the SGARAs*

Responses were received on 5 main types of SGARAs:

- Grape vines – Bearer SGARAs;
- Livestock – Consumable SGARAs;
- Forests / Plantations – Consumable SGARAs;
- Orchards / Trees – Bearer SGARAs; and
- Fruits / Nuts – Consumable SGARAs.

The majority of these SGARAs would be within the scope of IAS 41. SGARAs under operating lease (e.g. some grape vines) are outside the scope of IAS 41 and would be required to apply lease accounting.

The majority of respondents do not split the value of the SGARA into current and non-current components. Where the split is done, the current component comprises the amount expected to be consumed or realised (through sale) in the next 12 months (or operating cycle of the entity). Reference is made to budgets and a review against previous years' sales is made in auditing the split.

<sup>4</sup> Audit / Review of Financial Reports of entities with SGARAs

<sup>5</sup> Independent valuation of SGARAs to verify entity-determined values or for due diligence purposes

<sup>6</sup> Valuation of SGARAs for financial reporting purposes on behalf of entities with SGARAs

**General Comments***(sorted by ID)*

Submission	Comment	General comments
AV-4 <i>fm</i>	Greater clarity between operating and financing lease treatment is required. In addition, the impact of a contract for produce at a price exceeding market prices applicable at the end of the reporting needs to be dealt with.	
AV-10 <i>fm</i>	<p>The nature of audit evidence to support the validity of assumptions used causes concern. Similar evidence could equally be used to support variations with significant impact on the reported result e.g. varying the discount rate by a very small amount can often have a significant impact on net present value calculations.</p> <p>Both AASB 1037 and IAS 41 are concerned with valuations based on prospective information. ASIC has already raised concerns regarding the audit of prospective information provided in fund raising documents. In substance, information provide by applying AASB 1037 or IAS 41 is no different but, in contrast, is subject to high-level audit assurance.</p> <p>This type of information will cause an expectation gap where users do not fully understand the complexities of the calculations and the implications of changes in value arising through variation of the assumptions used.</p> <p>These standards only provide indicative financial information regarding performance.</p> <p>Major issues regarding the Standards are:</p> <ul style="list-style-type: none"> <li>• lack of rigour in some (so called) industry experts' valuation models;</li> <li>• determination of land value as separate from a long-term SGARA; and</li> <li>• selection of an appropriate discount rate.</li> </ul>	
AV-24 <i>fm</i>	<p>Comments concerning AASB 1037:</p> <ul style="list-style-type: none"> <li>• what is included in SGARA revenue? It appears that companies are duplicating revenue because they are accounting for the change in SGARA as revenue as well as sales of product as revenue (effectively the change in SGARA becomes part of the sale of the product down the track);</li> <li>• implementation issue with the Australian standard as to whether the standard retrospectively applied to existing inventory at the date of implementation (i.e. inventory resulting from previous living assets)<sup>7</sup>. There was inconsistency between the wine companies on this issue. Some wine companies uplifted the value of inventory as at the implementation date (and this adjustment went to opening retained earnings) others did not. Those companies that did uplift the value of inventory would have reduced gross margin going through the P&amp;L post implementation of the accounting standard. At the time of</li> </ul>	

<sup>7</sup> The transitional provisions in AASB 1037 / AAS 35 paragraph 9.1 required "Where the accounting policies required by this Standard are not already being applied as at the beginning of the financial year to which this Standard is first applied, they must be applied as at that date. Where this gives rise to initial adjustments which would otherwise be recognised in the profit and loss statement, the net amount of those adjustments, including any adjustments to deferred income tax balances, must, in accordance with Accounting Standard AASB 1018 [AAS 1] "Profit and Loss Accounts", be adjusted against retained profits or accumulated losses at the beginning of the financial year in which this Standard is first applied."

Submission	Comment	General comments
	<p>implementation it was our opinion that the Australian standard was vague as to whether it required companies to uplift the value of inventory;</p> <ul style="list-style-type: none"> <li>• analysts and others discount the effect of SGARA because it is non cash and brings inventories and other assets to a current valuation basis. The effect of the standard on B/S, P&amp;L and Cash Flow required a lot of explanation when it was first implemented because analysts and investors didn't understand it. Analysts and investors focus more and more on the importance of cash flows. <ul style="list-style-type: none"> <li>○ certain companies now report EPS and other KPIs on a normalised basis (i.e. before accounting for SGARA); and</li> <li>○ difficult to understand the difference between the effect on revenue and P&amp;L, especially when the standard has been in place for a number of years.</li> </ul> </li> </ul>	



## Specific Comments

### *Measurement and Recognition*

#### Valuation methods for different types of SGARAs

#### **Summary (including general information on problems in valuation or auditing)**

- The following significant issues have been encountered by respondents in applying the AASB 1037 / AAS 35 requirements:
  - separating other related assets e.g. trellising and irrigation systems;
  - annual crops – at half year end yield, quantity and quality are estimated even before fruit is starting to develop. Although calculations smooth seasonal variations, the level of reporting risk does not seem warranted given that actual crop will be known by the year end. Valuation of the SGARA as separate from the valuation of bare land continues to be an arbitrary estimation process;
  - identification of market value, different markets (geographical location) and change in market prices;
  - audit or the significant judgment exercised by client management in determining NMV of various categories of livestock assets;
  - valuation of timber plantation;
  - lack of vigour in valuation models used by industry experts; determination of the appropriate discount rate; separation of land from combined value of land and SGARA;
  - when native forests are managed on a sustainable basis, a factor had to be determined and applied to calculate the timber available for sale at the time of valuation. This required considerable discussions and effort from both client and auditor;
  - determining and eliminating restricted forests for SGARA valuation purposes; and
  - the Standard is considered impractical and requires a lot of effort (out the systems and processes of preparers) to derive the valuations.
- The following problems have arisen in making valuations or auditing valuations of the NMV of SGARA:
  - if cost is utilised for a vineyard just planted, the effect of tax deductions already used must be considered when assessing added value in relation to cost;
  - ability to factor in an appropriate measure of risk of crop failure. Estimation of prices depends on:
    - Australian harvests of Australian growers (i.e. weather, harvesting conditions etc);
    - harvest of global producers (weather, harvesting conditions in overseas locations); and
    - external economic indicators such as interest rates and exchange rates, e.g. estimated price for Australian crop may depend on climatic conditions in California during harvest period or actions of a stockpiler in India; and
    - Ability to make a reliable estimate is arbitrary;

- cost or transport to market;
- it can be difficult to obtain sufficient appropriate audit evidence to support NMVs determined by management because of the multiple (and sometimes conflicting) price indicators in the market;
- separation of the value of land from the combined value of land and SGARA. Justification for changes in assumptions;
- a number of assumptions are used in the valuation process, some derived from historical data, and these should be reviewed and validated. This requires wider industry and forestry knowledge to audit SGARA valuation;
- determination of NMV of SGARAs can be very subjective and difficult to determine at certain times of the year eg at the half year reporting periods the grape vines have partly formed grapes on them. It is difficult to value the partly formed grapes especially when you consider the risks the grapes will reach full maturity due to poor weather conditions and other associated risks. It allows companies to be quite conservative in their application of NMV; and
- accounting for SGARAs at NMV can give you NRV issues when the SGARA forms part of inventory.
- The majority of respondents did not identify additional problems in valuing the SGARA under IAS 41. However one respondent (AV-10) believed that IAS 41 is less prescriptive than AASB 1037 and is more open to interpretation.
- The main valuation methods used for the different types of SGARAs are:
  - Grape vines – Net present value (2 out of 2 entities);
  - Livestock – Net market value of the asset in an active and liquid market (1 entity) and Net market prices for similar and related assets (1 entity);
  - Forests / Plantations – Net present value (2 out of 3 entities);
  - Orchards / Trees – Net present value (for mature trees) and Cost (for immature trees) (1 entity);
  - Fruits / Nuts - Net market value of the asset in an active and liquid market (1 entity);
- Based on the 5 respondents that provided information regarding different types of SGARAs:
  - 4 respondents believed that their SGARA(s) can be valued reliably on a consistent basis at each reporting using the valuation methods that they apply; and
  - 1 respondent (Pitcher Partners) had mixed views believing forest valuations are reliable, however valuations of grape vines, orchards and crops are possibly not reliable.

**Comments extracted from submissions**

(sorted by position then ID)

Submission	Valuation method - AASB 1037 / AAS 35 (B2) <sup>8</sup>	Information on AASB 1037 / AAS 35 valuation (B2)	Valuation method - IAS 41 (B4) <sup>9</sup>	Information on IAS 41 valuation (B4)	Difference between valuation methods (B4, B5)	Reliable valuation - AASB 1037 (B1(e)(i), (ii))	Reliable valuation - IAS 41 (B1(f)(i), (ii))
<b>GRAPE VINES</b>							
AV-4 <i>Fin</i>	Net market prices for similar or related assets (b)	Sales of vineyards with price disaggregated into components.	Market prices for similar or related assets (c)	Sales of vineyards with price disaggregated into components.	No	Yes	Yes
AV-10 <i>Fin</i>	Net market value of the asset in an active and liquid market (a)	Prices published by major wine producers. Vineyards traded regularly.	Market value of the asset in an active and liquid market (a)	Prices published by major wine producers. Vineyards traded regularly.	No	Possibly Not	Possibly Not
<b>LIVESTOCK</b>							
AV-8 <i>General</i>	Net market value of the asset in an active and liquid market (a)	Cattle sales - published sale yard prices.	Market price of the asset in an active and liquid market (a)	Cattle sales - published sale yard prices.	No	Yes	Yes
AV-11 <i>General</i>	Net market prices for similar and related assets (b)	There are a number of price indicators in	Market prices for similar or related assets (c)	There are a number of price indicators in	No	Yes	Yes

<sup>8</sup> The letter beside the valuation method represents the valuation method identified in Question B2 of the Auditor / Valuer Questionnaire (refer to SGARAs Strategy, Paper).

<sup>9</sup> The letter beside the valuation method represents the valuation method identified in Question B4 of the Auditor / Valuer Questionnaire (refer to SGARAs Strategy, Paper).

Submission	Valuation method - AASB 1037 / AAS 35 (B2) <sup>1</sup>	Information on AASB 1037 / AAS 35 valuation (B2)	Valuation method - IAS 41 (B4) <sup>2</sup>	Information on IAS 41 valuation (B4)	Difference between valuation methods (B4, B5)	Reliable valuation - AASB 1037 (B1(e)(i), (ii))	Reliable valuation - IAS 41 (B1(f)(i), (ii))
	related assets (b)	indices maintained for livestock that provide guidance to net market value. A combination of indices, market prices and sales price data are used to determine a net market value. The existence of a number of sources of price information usually leads to a narrow range of acceptable net market values.	assets (c)	indices maintained for livestock that provide guidance to net market value. A combination of indices, market prices and sales price data are used to determine a net market value. The existence of a number of sources of price information usually leads to a narrow range of acceptable net market values.		number of price indicators in the marketplace (including the client's own sales) that provide reasonable guidance as to the NMV of livestock assets. However, there is judgment involved in determining the final price used.	models are consistent with the guidance outlined in IAS 41.18.
<b>FORESTS / PLANTATIONS</b>							
AV-8 <i>Perennial</i>	Net present value (d)	Risk - discount rate	Net present value (e)	Risk - discount rate	No	Yes	Yes
		Discount rate - WACC, Pre tax		Discount rate - WACC		Has been reliable in previous years.	
		50 year cash flow		50 year cash flow			

Submission	Valuation method - AASB 1037 / AAS 35 (B2) <sup>a</sup>	Information on AASB 1037 / AAS 35 valuation (B2)	Valuation method - IAS 41 (B4) <sup>b</sup>	Information on IAS 41 valuation (B4)	Difference between valuation methods (B4, B5)	Reliable valuation - AASB 1037 (B1)(e)(i), (ii)	Reliable valuation - IAS 41 (B1)(f)(i), (ii)
AV-10	Net present value (d)	Risk in combination of discount rate and cash flows.  Discount rate - Industry benchmark, Pre- tax.  Approx 20 (max) year cash flow	Net present value (e)	Risk in combination of discount rate and cash flows.  Discount rate - Industry benchmark, Pre- tax.  Approx 20 (max) year cash flow	No	Yes  There is an inherent uncertainty in the assumptions used as they are dependent on evaluations of future external economic factors	Yes  There is an inherent uncertainty in the assumptions used as they are dependent on evaluations of future external economic factors
		projections  Future growth - no growth rate applied throughout forecasted cash flows as an entity assumes that the most relevant and reliable information to hand on what cash flows will be incurred and will eventuate are the current plantation costs and current sale prices.		projections  Future growth - no growth rate applied throughout forecasted cash flows as an entity assumes that the most relevant and reliable information to hand on what cash flows will be incurred and will eventuate are the current plantation costs and current sale prices.			

Submission	Valuation method - AASB 1037 / AAS 35 (B2) <sup>g</sup>	Information on AASB 1037 / AAS 35 valuation (B2)	Valuation method - IAS 41 (B4) <sup>g</sup>	Information on IAS 41 valuation (B4)	Difference between valuation methods (B4, B5)	Reliable valuation - AASB 1037 (B1(e)(i), (ii))	Reliable valuation - IAS 41 (B1(f)(i), (ii))
		<p>projections.</p> <p>Future growth – expected yields based on growth patterns.</p>		<p>projections.</p> <p>Future growth – expected yields based on growth patterns.</p>		<p>(e.g. interest rates, demand) in addition to expected yields (quantities and quality). However, if the valuation model selected is applied consistently it will provide indicative measures about performance during the period and about relative performance from one period to the next. Therefore information may be considered reliable in relative terms but not as an absolute measure in any one year. Audit of these results can only provide</p>	<p>(e.g. interest rates, demand) in addition to expected yields (quantities and quality). However, if the valuation model selected is applied consistently it will provide indicative measures about performance during the period and about relative performance from one period to the next. Therefore information may be considered reliable in relative terms but not as an absolute measure in any one year. Audit of these results can only provide</p>

Submission	Valuation method - AASB 1037 / AAS 35 (B2) <sup>a</sup>	Information on AASB 1037 / AAS 35 valuation (B2)	Valuation method - IAS 41 (B4) <sup>b</sup>	Information on IAS 41 valuation (B4)	Difference between valuation methods (B4, B5)	Reliable valuation - AASB 1037 (B1(e)(i), (ii))	Reliable valuation - IAS 41 (B1(f)(i), (ii))
AV-12 (Planted forests, native forests) <i>Row</i>	Net market value of the asset in an active and liquid market (a) Cost (e) (for young plantations < 15 years)	Timber supply agreements are entered into with mill customers based upon standing volumes and current prices less the direct costs of disposing of the timber. Young plantations (<15 years) have no realistic market and cost is the best indicator.	Net market value of the asset in an active and liquid market (a) Cost (f) (for young plantations < 15 years)	Timber supply agreements are entered into with mill customers based upon standing volumes and current prices less the direct costs of disposing of the timber. Young plantations (<15 years) have no realistic market and cost is the best indicator.	No	Yes There are measures available to determining the quantity and net market value of produce derived from these SGARAs.	Yes There are measures available to determining the quantity and net market value of produce derived from these SGARAs.
a minimal level of assurance.							
a minimal level of assurance.							
ORCHARDS / TREES							
AV-10 <i>Row</i>	Net present value (d) (for mature trees) Cost (e) (for immature trees)	Risk in combination of discount rate and cash flows. Discount rate – asset specific risk adjusted, Pre-tax.	Net present value (e) (for mature trees) Cost (f) (for immature trees)	Risk in combination of discount rate and cash flows. Discount rate – asset specific risk adjusted, Pre-tax.	No	Possibly Not Consistent only in terms of applying probability to assumptions / estimates.	Possibly Not Consistent only in terms of applying probability to assumptions / estimates.

Submission	Valuation method -AASB 1037 / AAS 35 (B2) <sup>8</sup>	Information on AASB 1037 / AAS 35 valuation (B2)	Valuation method -IAS 41 (B4) <sup>9</sup>	Information on IAS 41 valuation (B4)	Difference between valuation methods (B4, B5)	Reliable valuation -AASB 1037 (B1)(c)(i), (ii)	Reliable valuation -IAS 41 (B1)(f)(i), (ii)
		10 year cash flow projections. Future growth – yields based on age. Risks in cash flows – agri-risk, market risk. Immature trees that are not bearing fruit (i.e. young orchards) are carried at cost to grow and maintain until they are mature.		10 year cash flow projections. Future growth – yields based on age. Risks in cash flows – agri-risk, market risk. Immature trees that are not bearing fruit (i.e. young orchards) are carried at cost to grow and maintain until they are mature.			
<b>FRUITS / NUTS</b>							
AV-10 (Crops)	Net market value of the asset in an active and liquid market (a)	Global nut market.	Market price of the asset in an active market (a)	Global nut market.	No	Possible Not Consistent only in terms of applying probability to assumptions / estimates.	Possible Not Consistent only in terms of applying probability to assumptions / estimates. Less reliable than waiting for actual results when a



Submission	Valuation method - AASB 1037 / AAS 35 (B2) <sup>4</sup>	Information on AASB 1037 / AAS 35 valuation (B2)	Valuation method - IAS 41 (B4) <sup>5</sup>	Information on IAS 41 valuation (B4)	Difference between valuation methods (B4, B5)	Reliable valuation - AASB 1037 (B1(e)(i), (ii))	Reliable valuation - IAS 41 (B1(f)(i), (ii))
						crop is harvested annually.	crop is harvested annually.
						In the case of annual crops AASB 1037 brings forward recognition of profits inappropriately.	In the case of annual crops IAS 41 brings forward recognition of profits inappropriately.
							For annual crops actual harvest yield will be known within each 12 month period. It is unnecessary to bring forward revenue using potentially unreliable estimates in situations where the magnitude of error could be large e.g. if the harvest fails through crop damage.

SGARAs accounting versus lease accounting

Summary

Only one respondent (AV-10) provided a response on whether SGARAs accounting provides more useful information than lease accounting. The respondent expressed the view that SGARA accounting is a highly subjective exercise. The appropriate interpretation of performance thus reported depends on the users background knowledge. For less sophisticated users, operating lease payments provide an objective, definitive measure.

***Scope of Standards*****Special industry / entity features****Summary**

Six respondents provided a response on whether there are special features associated with particular industries or operations of particular entities in which additional problems or issues arise in valuing and / or auditing valuations of SGARAs made in accordance with AASB 1037 / AAS 35 and / or IAS 41. Three respondents identified additional problems associated with annual crops, native forests and the SGARAs of wine companies. Three respondents specifically stated that there are no special features.

**Comments extracted from submissions***(sorted by position then ID)*

<b>Submission</b>	<b>Comment</b>	<b>Special industry / entity features</b>
AV-10 <i>W</i>	Annual crops – SGARAs accounting provides less reliable information than historical cost.	
AV-12 <i>General</i>	Native forests need to be managed on a sustainable basis taking into account flora, fauna, habitat etc. This makes it difficult to determine the standing timber available for harvesting at any point in time.	
AV-24 <i>W</i>	The wine companies would argue that SGARA should specifically exclude grape vines/grapes and that it should apply solely to assets such as forest plantations which are considered to be fundamentally different to grape vines/grapes.	

***Presentation and Disclosure*****Disclosure Requirements****Summary**

Two out of three respondents to whether there are specific issues on the disclosure requirements in AASB 1037 / AAS 35 believed that they were too complex and extensive or had difficulty in obtaining the information. Four out of the five respondents on whether there are any specific issues on the disclosure requirements in IAS 41 had no specific issues. The other respondent believed that the disclosures were too complex or extensive.

**Comments extracted from submissions***(sorted by position then ID)*

<b>Submission</b>	<b>Comment</b>	<b>Disclosure Requirements</b>	
		<b>AASB 1037 / AAS 35 Disclosures</b>	<b>IAS 41 Disclosures</b>
AV-4 <i>fin</i>	No specific issues.	No specific issues.	No specific issues.
AV-8			No specific issues.
AV-10 <i>h</i>	Disclosures can be complex and extensive. It is often difficult to balance sensitivity and usefulness with the presentation of extensive notes. Dependent on the nature and extent of disclosures about assumptions, competitors and customers have access to key market expectations that might impact on management strategy.		Disclosures can be complex and extensive. It is often difficult to balance sensitivity and usefulness with the presentation of extensive notes. Dependent on the nature and extent of disclosures about assumptions, competitors and customers have access to key market expectations that might impact on management strategy.
AV-11			No specific issues.
AV-12	Yes – difficulty in obtaining the information.  Where the biological assets are not homogenous by species, it is difficult to disclose meaningful information by species.		No specific issues.

## Users

### General

#### General information about the respondent

(sorted by ID)

Submission	Interest in SGARAs
U-2	Conservation Group
U-3 <i>Roberts</i>	Academic (contributor to Discussion Paper 23 "Accounting for Self-Generating and Regenerating Assets" (1995))
U-6 <i>Auditor General</i>	Assessing the stewardship of Tasmanian State forests by the Tasmanian Forestry Corporation (Forestry Tasmania) for the purpose of public and parliamentary scrutiny and policy and commercial accountability.
U-7	Academic
U-9	Representative body for users

#### General Comments

(sorted by ID)

Submission	Comment	General comments
U-2	<p>The application of AAS 35 does not give a true picture of profitability for native forests.</p> <p>I refer to the accounts of the Forest Products Commission (WA). The FPC reported a profit from ordinary activities before grants and subsidies of \$5m. Making up this was a revaluation of the native forest standing timber of \$66m, i.e. before applying AAS 35 to the native forest standing timber the FPC would have reported a loss of \$61m. The application of AAS 35 completely overwhelms the profit / loss result. The FPC provides a sensitivity analysis, which concludes that for each 1% change in the future income stream the impact of the NPV is \$67m. By a very minor stroke of the pen, by the slightest wobble in preparing the cash flow on which to value the SGARA the profit / loss picture for the FPC will change dramatically.</p> <p>The application of AAS 35 probably does not provide a reliable measurement. For the FPC's 2001 year end their native forest standing timber (SGARAs) were valued at \$0. That is the entire loggable forest estate of WA was valued at nothing in accounts signed by the directors and the Auditor-General. Clearly this is wrong. Native forest logs in WA are sold well below market value and there is the real possibility of greatly increasing royalties – even by a magnitude of up to 5 times. Assume they increase by 100%, then the profit for the year of increase would increase by \$6.7 billion (other things being equal and according to the FPC sensitivity analysis), but the following year, making the same assumptions, return to \$0. Such a result would not give a true picture of operations.</p> <p>AAS 35 would seem not to be applicable in many cases, but when a corporation is "given" its main asset, as in the case of native forests, it would seem that there are a lot of shortcomings with the standard. It would seem that (assuming costs and prices remain the same) the only way of making a profit from native forestry is to log at a rate less than the forest</p>	

Submission	Comment	General comments
U-3	<p>I am absolutely convinced that IAS 41 does not deal properly with profit of loss in self-generation and regeneration.</p> <ol style="list-style-type: none"> <li>1. SGARAs are unique (see ED 83 paragraph 1, page 1)</li> <li>2. The reason for IAS 41 is to prescribe accounting standards to accommodate the unique characteristics of SGARAs.</li> <li>3. ED 114 page 18 – Changes in fair value are brought about through both biological change and changes in prices. To include price changes as part of operating profit virtually corrupts the financial measurement of profits and losses due to self-generation and regeneration.</li> </ol>	
U-9	<p>It is worth making the point in view of the trend towards incorporation of accretions to asset values into income, often using estimates of future values of the sort adopted in AASB 1037 / AAS 35 and IAS 41.</p> <p>The entity's concern is the classification of value increments as income without prescribing an obligation to disclose realised and unrealised components of income separately. The notion of realisation of income through the objective test of arm's length market transactions (including fixed-price forward contracts) remains meaningful as an indicator of the nature and quality of income measurement. Measurement of income using prospective sale values minus estimates of costs to completion yields useful information, but it is information of a vastly different nature and quality from realised income. Reports that fail to distinguish realised and unrealised components of income fail to meet the information needs of investors in companies. If forced to choose between reports of total income comprising all value increments, and reports of realised income, the entity's members would clearly prefer the latter.</p> <p>It would be useful to have both. The method in mark-to-market accounting by UK investment entities, involving showing value increments in three columns (Realised, Unrealised and Total) might have more general application.</p>	

**Specific Comments*****Measurement and Recognition*****SGARAs accounting versus lease accounting****Summary**

Only one respondent (U-7) provided a response on whether SGARAs accounting provides more useful information than lease accounting. The respondent expressed the view that SGARAs accounting is more useful because capitalisation of executory contracts, is in his opinion, based on a misconception relating to profit measurement.

***Scope of Standards*****Exclude from scope of AASB 1037 / AAS 35 and IAS 41****Summary**

Two respondents provided a response on whether there are SGARAs (under AASB 1037 / AAS 35) and biological assets (under IAS 41) that are included in their respective scopes that should be excluded. One respondent believed that AASB 1037 / AAS 35 should not apply to old-growth forest SGARAs held for clearing. The other respondent believed that there all SGARAs should be included in the scope of AASB 1037 / AAS 35.

The two respondents did not believe that there are any biological assets that should be excluded from the scope of IAS 41. The respondent that expressed concern that old-growth forest SGARAs held for clearing should be excluded under AASB 1037 / AAS 35 believed that the definition of agricultural assets under IAS 41 is more robust than that under AASB 1037 / AAS 35, particularly because of its exclusion of deforestation from the Standard (paragraph 6(b)) on the grounds that this does not represent agriculture (unlike management of plantations and regrowth forests) but rather represents extraction.

**Comments extracted from submissions***(sorted by position then ID)*

<b>Submission</b>	<b>Comment</b>	<b>Exclude from scope of AASB 1037 / AAS 35</b>
U-6 <i>Auditor General</i>	<p>AASB 1037 applies to SGARAs held <i>primarily for profit</i> and not to SGARAs held for the <i>primary purposes of aesthetics, heritage, ecology, the environment, or recreation</i>.</p> <p>Furthermore, it should not apply to old-growth forest SGARAs held for clearing the conversion to other users. Old-growth forests have the following characteristics:</p> <ol style="list-style-type: none"> <li>1. Once “harvested” it is not replaced (it takes hundreds of years to fully regenerate an old-growth forest – while current management regimes require conversion of old-growth to managed regrowth or plantation regimes on rotations of mere decades at most). This is not a renewable use of the resource when converted in this way.</li> <li>2. It has enormous value as a carbon store and carbon sink with long term potential as a source of value for carbon credits that should outweigh the value of a one-off extraction under current management regimes.</li> <li>3. It is viewed by the community as having a very high aesthetic, environmental, existence and recreational value. (In 2001, 80% of Tamanians indicated support for a cessation of clearfelling of the last of their old-growth forests.)</li> </ol> <p>Destruction of old-growth (which is eventually replaced with very different and much less valuable SGARAs) should not be reported under AASB 1037. The characteristic of these assets is much more akin to extractive mining or to the run off of an embedded value of life insurance policies. It should be separately disclosed and accounted for so that the impact of liquidation of old-growth resources and associated loss of value can be judged separately from the normal commercial operations of renewable plantations and regrowth forests harvesting for commodity wood production for industrial supply.</p> <p>The appropriate valuation method for old-growth forest is a “best and highest use” valuation method which also recognises the value of the old-growth forest as a carbon sink, an environmental asset, a recreational asset, an</p>	



Submission	Comment	<i>Exclude from scope of AASB 1037 / AAS 35</i>
	<p>aesthetic asset and a source of unique "speciality timbers". While Forestry Tasmania's corporate charter states that forests are managed for these multiple purposes, the application of AASB 1037, which values only the one off extraction of logs for timber and woodchips, gives a profoundly misleading view of our stewardship of the forests. "Best and highest use" is the method gaining currency in the US for valuing their state old-growth forests.</p> <p>At present, AASB 1037 has been applied in a manner which purposefully confuses and obfuscates the accounts as a tool for measuring the performance of state-owned forestry companies, like Forestry Tasmania, against their multiple objectives.</p> <p>Old-growth forests and reserved forests, which are simply not capable of being subject to sustainable management for renewable commodity wood resource supply purposes, should not be bundled inside the SGARA valuation but should be shown separately in the segmented results. This is not currently being done. For example, in the case of Forestry Tasmania, the forest asset attributable to such non-SGARA assets is separately identified in the accounts in terms of hectares but not in terms of value. This means that measuring the true SGARA return is impossible.</p>	

Include in scope of AASB 1037 / AAS 35 and IAS 41

**Summary**

Only one respondent (U-7) provided a response on whether there are SGARAs (under AASB 1037 / AAS 35) and biological assets (under IAS 41) that are excluded from their respective scopes that should be included. The respondent did not believe that there were any additional SGARAs to be included in the scope of AASB 1037 / AAS 35, however believed that the scope of IAS 41 should be expanded to be the same as AASB 1037 / AAS 35.

**Special industry / entity features**

**Summary**

Two respondents provided a response on whether there are special features associated with particular industries or operations of particular entities in which SGARAs accounting does not provide relevant and reliable information to users of accounts. One respondent noted that state forestry corporations have been unable to apply AASB 1037 without material errors in the calculation of SGARA and that this affects the usefulness of the information. This respondent also questions the usefulness of the assessment of stewardship of SGARA assets. The other respondent did not believe there were any special features.

**Comments extracted from submissions**

*(sorted by position then ID)*

<b>Submission</b>	<b>Comment</b>	<b>Special industry / entity features</b>
U-6	<i>Errors in valuation models</i>	
<i>Auditor's found</i>	<p>It appears that state forestry corporations have been unable to apply AASB 1037 without material errors in the calculations of the SGARA value. This has resulted in profits being reported with over 50% errors and a flow through error in the following years' accounts. In the context of large errors, the question of whether AASB 1037 is useful becomes irrelevant. The errors since the introduction of AASB 1037 have greatly lessened users' confidence in the accounts. Given the complexity of many of the models that determine the SGARA valuation, it seems vital that the SGARA valuation models are not only independently developed and maintained but also independently signed out, rather than included at Directors' valuation. We believe such transparency and independence should be mandated as part of AASB 1037 for large companies and long rotation agricultural assets (of, say, more than five years between establishment and harvest).</p> <p><i>Assessing stewardship of SGARA assets</i></p> <p>AASB 1037 states that measuring SGARAs at net market value provides a relevant basis for "assessing stewardship of the entity's management by indicating the effects of the decisions to buy, sell or hold SGARAs". Unfortunately, this is true only when the original valuation of SGARAs reflects good stewardship.</p> <p>Forestry Tasmania (and the Forestry Commission before it) has come under sustained criticism not only for its poor financial management in failing to meet the goals set for it by government but also for its poor resource management. In particular, a number of reports have indicated extraordinary levels of waste. In one independent study, 74% of the timber volume of a clearfelled coup in old-growth wet mixed (eucalypt and rainforest) forest was</p>	

Submission	Comment	<i>Special industry / entity features</i>
	left behind and subsequently burned.	
	The economic impact of such waste is not evident in the accounts, however, because the waste was “pre-planned” in the SGARA valuation. In other words, the net present value calculation assumes that significant volumes of valuable wood will be burned, because this is the current management regime.	
	Because of a drive to fulfil contracts for export hardwood chips, special species timbers are also felled at a rate faster than they can be sold. Left standing, old-growth speciality timbers have a very high net present value but, cut down in such large volumes, they create a glut today of old timbers that face declining future supply and likely commercial extinction within a few decades.	
	The SGARA forest valuation model used by Forestry Tasmania assumes that a high percentage of these specialty timbers are left behind and burned after clear felling of the coup, when forecasting the value of each old-growth coup. Thus the loss of economic value of wood resources is not reflected in the accounts.	
	No attempt is made to identify, let alone quantify, other sources of value of native forests, especially of old-growth forests subject to ongoing conversion to managed tree farms (seeded regeneration and plantations).	
	As things are today, the stewardship of the State’s publicly-owned and managed native forests cannot be measured.	

***Presentation and Disclosure*****Presentation of revenues and expenses from SGARAs****Summary**

Only one respondent (U-7) commented on how information relating to SGARAs should be presented to provide the most meaningful information to users. This respondent believed that for the assumed purpose of money capital maintenance, profit measurement should be based on executed sales contracts (i. e. this would capture realised profits).

## Disclosure Requirements

### Summary

Two respondents commented on whether the disclosure requirements in AASB 1037 / AAS 35 and IAS 41 provide useful information to users of the accounts. The respondents raised the following issues on disclosures:

- failure to separate asset types, disclose sensitivities and assumptions under AASB 1037 / AAS 35;
- requirement to separately disclose biologically mature versus biologically immature assets under IAS 41;
- both cost based amounts (for profit measurement) and current market selling prices (for wealth measurement) should be separately disclosed under AASB 1037 / AAS 35 and IAS 41.

### Comments extracted from submissions

*(sorted by position then ID)*

<u>Submission</u>	<u>Comment</u>	<u>Disclosure Requirements</u>
U-6 (AASB 1037/ AAS 35 Disclosures)	<p><i>Failure to separate asset types</i></p> <p>The requirement in paragraph 7.1(b) that SGARAs with restricted sale potential be separately disclosed in being flouted by state-owned forestry corporations, and this is part of what makes AASB 1037 so difficult to use for our purposes. For example, Forestry Tasmania manages both reserves (i.e. cannot be harvested) and non-reserved land. It does not separately disclose the component of the land value and SGARA value attributable to each.</p> <p>Without separation of the land value and the SGARA value for these separate tranches, it is impossible to know what commercial return is being achieved on the non-reserved land.</p> <p>A further separation should also be required between “old-growth” and plantations and regrowth forests. This is the difference between assets which are truly SGARAs, such as plantations and forests, and those which cannot be renewed, such as old-growth forests, including rainforests. AASB 1037 does not require separate disclosure of these very different types of situations.</p> <p><i>Failure to disclose sensitivities</i></p> <p>The state-owned forestry corporations do not disclose sensitivities of the SGARA valuation, although the standard “encourages” this. Because the financial return being achieved by the forestry companies is under debate, such sensitivities are vital to informed public debate and effective Parliamentary scrutiny. In discussions with Forestry Tasmania, we have been forced to “retro-build” a model to enable rough sensitivities to be determined.</p> <p>This non-disclosure of sensitivities is in contrast to other financial reporting involving the forecasting of future cash flows, for example in prospectuses or in the accounts of financial services companies carrying assets at embedded value in the balance sheet.</p> <p><i>Failure to disclose assumptions</i></p> <p>Paragraph 7.1(c)(ii) requires that companies disclose “any significant assumptions made in determining the net market values” of the SGARAs.</p>	

Submission	Comment	Disclosure Requirements
	<p>AASB 1037 should include a requirement that the disclosure of significant assumptions actually says what they are, rather than just saying they have been set in accordance with the standard. Insofar as GBEs are not subject to independent scrutiny by professional analysts in the same way that publicly listed companies are, there is a real danger that the persistent and undisclosed use of inflated future price assumptions to bolster apparent returns by a bureaucratic management culture persisting from the days before notional corporatisation could get a future government, as owner of both the resource and the business, into real trouble.</p>	
<p>U-6 (IAS 41 Disclosures)</p>	<p>The requirement under IAS 41.43 to disclose biologically mature assets separately from immature assets is based on an assumption that does not hold for the agricultural management of tree crops to be harvested for industrial wood production. Such crops are managed to be harvested at a biologically immature stage of development. Commercial maturity occurs a relatively long time before biological maturity for both solid wood (timber) and wood fibre (pulp) production. This is not an artefact of the cost money, but recognition that the intended commercial crop is young wood (especially production of young wood fibres for optimal pulping qualities).</p>	
<p>U-7 (AASB 1037/ AAS 35 and IAS 41 Disclosures)</p>	<p>I believe that both cost based amounts (for profit measurement) and current market selling prices (for wealth measurement) should be separately disclosed. In addition, the disclosure of quantitative and qualitative information should enable users to calculate future maintainable profit for their decision models.</p>	

*Simon de Bussan*

