

## IAS 41 - QUESTION

A public limited company, Dairy, produces milk on its farms. It produces 30% of the country's milk that is consumed. Dairy owns 450 farms and has a stock of 210,000 cows and 105,000 heifers. The farms produce 8 million kilograms of milk a year, and the average inventory held is 150,000 kilograms of milk. However, the company is currently holding stocks of 500,000 kilograms of milk in powder form. At October 31, 20X4, the herds are

- 210,000 cows (3 years old), all purchased on or before November 1, 20X3
- 75,000 heifers, average age 1.5 years, purchased on April 1, 20X4
- 30,000 heifers, average age 2 years, purchased on November 1, 20X3

No animals were born or sold in the year.

The unit values less estimated point-of-sale costs were

	\$
1-year-old animal at October 31, 20X4:	32
2-year-old animal at October 31, 20X4:	45
1.5-year-old animal at October 31, 20X4:	36
3-year-old animal at October 31, 20X4:	50
1-year-old animal at November 1, 20X3 and April 1, 20X4:	30
2-year-old animal at November 1, 20X3:	40

The company has had problems during the year: Contaminated milk was sold to customers. As a result, milk consumption has gone down. The government has decided to compensate farmers for potential loss in revenue from the sale of milk. This fact was published in the national press on September 1, 20X4. Dairy received an official letter on October 10, 20X4, stating that \$5 million would be paid to it on January 2, 20X5. The company's business is spread over different parts of curtailed milk production in the region. The cattle were unaffected by the contamination and were healthy. The company estimates that the future discounted cash flow income from the cattle in the Mexico region amounted to \$4 million, after taking into account the government restriction order. The company feels that it cannot measure the fair value of the cows in the region because of the problems created by the contamination. There are 60,000 cows and 20,000 heifers in the region. All these animals had been purchased on November 1, 20X3. A rival company had offered Dairy \$3 million for these animals after point-of-sale costs and further offered \$6 million for the farms themselves in that region. Dairy has no intention of selling the farms at present. The company has been applying IAS 41 since November 1, 20X3.

### **Required**

**Advise the directors on how the biological assets and produce of Dairy should be accounted for under IAS 41, discussing the implications for the financial statements.**

## IAS 41 - SOLUTION

Biological assets should be measured at each balance sheet date at fair value less estimated point-of-sale costs unless fair value cannot be measured reliably. The Standard encourages companies to separate the change in fair value less estimated point-of-sale costs between those changes due to physical reasons and those due to price.

	<b>\$000</b>	<b>\$000</b>	
<b>Fair value of cattle excluding Mexico region:</b>			
Fair value at November 1, 20X3			
Cows (210,000 – 60,000) × \$40		6,000	
Heifers (30,000 – 20,000) × \$30		300	
Purchase 75,000 heifers × \$30		2,250	
		<b>8,550</b>	
Increase due to price change			
150,000 × \$(45 – 40)	750		
10,000 × \$(32 – 30)	20		
75,000 × \$(32 – 30)	150		
		<b>920</b>	
Increase due to physical change			
150,000 × \$(50 – 45)	750		
10,000 × \$(45 – 32)	130		
75,000 × \$(36 – 32)	300		
		<b>1,180</b>	
Fair value less estimated point-of-sale costs at October 31, 20X4			
150,000 × \$50	7,500		
10,000 × \$45	450		
75,000 × \$36	2,700		
		<b>10,650</b>	

### **Mexico region—fair value of cattle:**

This region has an inventory of cattle of 60,000 cows and 20,000 heifers. Fair value is difficult to ascertain because of the region's problems. However, according to IAS 41, if fair value was used on initial recognition, then it should be continued to be used. The cattle in this region would have been fair valued at November 1, 20X3, under the Standard. Therefore, the cattle must be valued at fair value less estimated point-of-sale costs as at October 31, 20X4. Although \$3 million has been offered for these animals, this may be an onerous contract as rival companies are likely to wish to take advantage of the problems in this region. The future discounted income is again an inappropriate value as the cattle are healthy and could be moved to another region and sold. The cattle in this region would therefore be valued at

	<b>\$000</b>	
60,000 cows × \$50	3,000	
20,000 heifers × \$45	900	
	<b>3,900</b>	