IFRS

STAFF PAPER

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IFRS® Interpretations Committee meeting

Project	**Subsequent expenditure on biological assets (IAS 41)**		
Paper topic	Initial Consideration		
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Introduction

1. The IFRS Interpretations Committee (Committee) received a submission about the accounting for costs related to the biological transformation of biological assets (subsequent expenditure) applying IAS 41 *Agriculture*. The submitter asked whether an entity (a) recognises subsequent expenditure as an expense when incurred, or (b) capitalises the subsequent expenditure (ie adds it to the carrying amount of the asset).

2. The objective of this paper is to:

   (a) provide the Committee with background information on the matter;

   (b) present our research and analysis; and

   (c) ask the Committee whether it agrees with our recommendation not to add the matter to its standard-setting agenda.

Structure of the paper

3. This paper includes:

   (a) background information;

   (b) outreach and additional research;

(c) staff analysis; and

(d) staff recommendation.

4. There are two appendices to this paper:

(a) Appendix A—proposed wording of the tentative agenda decision; and

(b) Appendix B—submission.

Background information

5. IAS 41 requires an entity to measure biological assets on initial recognition and at the end of each reporting period at fair value less costs to sell (FV), except in particular situations in which fair value cannot be measured reliably. The submitter asks how an entity accounts for subsequent expenditure on a biological asset measured at FV.

6. The submission outlines three possible views:

- View 1—recognise subsequent expenditure as an expense when incurred (hereafter, expense subsequent expenditure);
- View 2—capitalise subsequent expenditure; or
- View 3—either capitalise or expense subsequent expenditure (accounting policy choice).

7. The different views have no effect on the measurement of biological assets nor do they have any effect on profit or loss; however, as illustrated in the example below, they affect the presentation of amounts in the statement of profit or loss.

8. Appendix B to this paper reproduces the submission and provides further details on those views.

Example

9. Entity X has a biological asset measured at FV of CU200 as at 31 December 2017. During 2018, Entity X incurs expenditure of CU300 in growing the biological asset; the biological asset's FV at 31 December 2018 is CU600.

10. The following table illustrates the different outcomes of expensing or capitalising subsequent expenditure:

	Expense Subsequent Expenditure		**Capitalise Subsequent Expenditure**	
	Biological Asset Debit / (Credit)	Profit or Loss Debit / (Credit)	Biological Asset Debit / (Credit)	Profit or Loss Debit / (Credit)
FV, 31 December 2017	**CU200**		**CU200**	
Capitalise subsequent expenditure			CU300	
Expense subsequent expenditure		CU300		
Change in FV during the year	CU400	(CU400)	CU100	(CU100)
FV, 31 December 2018	**CU600**		**CU600**	
Effect on profit or loss		**(CU100)**		**(CU100)**

Outreach and additional research performed

Outreach

11. We sent information requests to members of the International Forum of Accounting Standard-Setters, securities regulators and large accounting firms.

12. The request asked those participating to provide information based on their experience about:

    (a) whether entities with biological assets incur material amounts of subsequent expenditure;

(b) if yes, how do such entities account for subsequent expenditure (ie do they capitalise or expense such expenditure)?

(c) if entities expense subsequent expenditure, in which line item(s) of the statement of profit or loss do they present subsequent expenditure?

13. We received 13 responses—seven from large accounting firms, four from national standard-setters and two from organisations representing groups of regulators. The views received represent informal opinions, rather than formal views of those responding.

Do entities incur material amounts of subsequent expenditure?

14. Several respondents said entities incur material amounts of subsequent expenditure on biological assets. In addition:

(a) some respondents said the amount of subsequent expenditure is likely to depend on the type of biological asset. For example, entities would not generally incur material amounts of subsequent expenditure on biological assets with a short harvesting period (usually two to three weeks), such as fresh fruit bunches. In contrast, entities would generally incur material amounts of such expenditure on biological assets with a long harvesting period (usually more than 12 months), such as timber and rubber.

(b) one respondent said cannabis producers incur material amounts of subsequent expenditure.

(c) one respondent said, for some entities, the amount of subsequent expenditure per biological asset might not be high, especially compared to fair value. However, it can be a material amount for all biological assets held by the entity.

15. Two respondents said entities in their jurisdictions do not generally incur material amounts of subsequent expenditure.

Accounting treatment applied

16. Almost all respondents who had experience with entities incurring subsequent expenditure observed mixed practice (ie some entities capitalise subsequent expenditure while others expense it). In addition,

(a) some respondents said practice is mixed even within the same industry. For example, one respondent said some grape producers in one jurisdiction capitalise subsequent expenditure while other grape producers expense it.

(b) one respondent said, in the fish farming industry, any increase in the attributes of biological assets is directly linked to the use of feed or medicine. No growth takes place without incurring expenditure and, thus, entities in that industry generally capitalise subsequent expenditure.

In which line item(s) of the statement of profit or loss is the subsequent expenditure presented?

17. Many respondents said the line item in which an entity presents subsequent expenditure depends on whether entities present expenses by nature or by function. Respondents said (a) entities that present expenses by function generally present subsequent expenditure either as cost of sales or as other operating expenses, and (b) entities that present expenses by nature generally present subsequent expenditure according to the nature of that subsequent expenditure.

Additional research performed

18. We reviewed the financial statements of 15 entities across nine jurisdictions with various types of biological assets. We found that entities do not generally disclose their accounting policy for subsequent expenditure—accordingly, it is difficult to assess:

(a) whether these entities incur material amounts of subsequent expenditure;

(b) whether they capitalise or expense subsequent expenditure; and

(c) if capitalised, which costs are capitalised.

19. Although not directly obvious, some entities appear to capitalise subsequent expenditure while others appear to expense it. Only one entity disclosed its accounting policy on subsequent expenditure.

20. In addition, we reviewed the report of the staff of the Canadian Securities Administrators (CSA), CSA staff notice 51-357, published in October 2018 (CSA Staff Notice). CSA staff reviewed disclosures of 70 entities operating in the cannabis industry. The staff note that 48% of entities capitalise subsequent expenditure while 52% expense it. CSA staff also note that entities did not clearly disclose whether they capitalise or expense costs directly and indirectly related to biological assets.

Staff analysis

Requirements in IAS 41

21. IAS 41 does not prescribe how to account for subsequent expenditure on biological assets measured at FV. Paragraphs B61–B62 of the Basis for Conclusions acknowledge this and state:

> B61. The Standard does not explicitly prescribe how to account for subsequent expenditure related to biological assets. E65 proposed that costs of producing and harvesting biological assets should be charged to expense when incurred and that costs that increase the number of units of biological assets owned or controlled by the entity should be added to the carrying amount of the asset.
>
> B62. Some believe that there is no need to capitalise subsequent expenditure in a fair value model and that all subsequent expenditure should be recognised as an expense. Some also argue that it would sometimes be difficult to prescribe which costs should be recognised as expenses and which costs should be capitalised; for example, in the case of vet fees paid for delivering a calf. The Board decided not to explicitly prescribe the accounting for subsequent expenditure related to

> biological assets in the Standard, because it believes to do so is unnecessary with a fair value measurement approach.

22. In the absence of requirements on accounting for subsequent expenditure in IAS 41, we think entities can either capitalise or expense subsequent expenditure.

23. Our view is confirmed by amendments made to IAS 23 *Borrowing Costs* in 2007. Those amendments excluded qualifying assets measured at fair value from the scope of the requirement in IAS 23 to capitalise borrowing costs. IAS 23 therefore permits an entity to either capitalise or expense borrowing costs directly attributable to such qualifying assets. Paragraph BC4 of IAS 23 explains the Board's rationale for this decision, referring to IAS 41. Paragraph BC4 states (emphasis added):

> …The measurement of such assets will not be affected by the amount of borrowing costs incurred during their construction or production period. Therefore, requirements on how to account for borrowing costs are unnecessary, *as paragraphs B61 and B62 of the Basis for Conclusions on IAS 41 Agriculture explain*. But the Board noted that the exclusion of assets measured at fair value from the requirements of IAS 23 *does not prohibit an entity from presenting items in profit or loss as if borrowing costs had been capitalised* on such assets before measuring them at fair value.'

Other considerations

Consistency in applying accounting policy

24. Paragraph 13 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* states:

> An entity shall select and apply its accounting policies consistently for similar transactions, other events and conditions, unless an IFRS specifically requires or permits categorisation of items for which different policies may be appropriate. If an IFRS requires or permits such categorisation,

> an appropriate accounting policy shall be selected and applied consistently to each category.

25. Accordingly, we think an entity applies its accounting policy for subsequent expenditure (ie to capitalise or expense subsequent expenditure) consistently to each group of biological assets. Paragraph 5 of IAS 41 defines a group of biological assets as ‘an aggregation of similar living animals or plants.’

Disclosure

26. Paragraphs 117-124 of IAS 1 *Presentation of Financial Statements* provide requirements for disclosures of accounting policies. In particular, paragraphs 117 and 119 of IAS 1 state:

> 117. An entity shall disclose its significant accounting policies comprising:
>
> (a) …
>
> (b) the other accounting policies used that are relevant to an understanding of the financial statements...
>
> 119. In deciding whether a particular accounting policy should be disclosed, management considers whether disclosure would assist users in understanding how transactions, other events and conditions are reflected in reported financial performance and financial position...Disclosure of particular accounting policies is especially useful to users when those policies are selected from alternatives allowed in IFRSs…

27. Applying these requirements, we think an entity would disclose its accounting policy for subsequent expenditure when that disclosure would assist users in understanding how subsequent expenditure is reflected in the entity’s reported financial performance.

28. Our research of public financial statements of entities with biological assets (see paragraphs 18–19 of this paper) identified a lack of disclosure about how entities account for subsequent expenditure. We think it could be helpful if the Committee were to highlight existing disclosure requirements in this respect.

Staff conclusion

29. Based on our analysis in paragraphs 21–28 of this paper, we conclude that:

    (a) applying IAS 41, an entity can either capitalise subsequent expenditure on biological assets measured at FV or recognise it as an expense when incurred;

    (b) applying paragraph 13 of IAS 8, an entity applies its accounting policy for subsequent expenditure consistently to each group of biological assets; and

    (c) applying paragraphs 117–124 of IAS 1, an entity discloses its accounting policy for subsequent expenditure when that disclosure assists users in understanding how subsequent expenditure is reflected in the entity's reported financial performance.

Question 1 for the Committee
1. Does the Committee agree with the staff analysis of the requirements in IFRS Standards outlined in paragraphs 21–29 of this paper?

Should the Committee add this matter to its standard-setting agenda?

30. As discussed in paragraph 7 of this paper, capitalising or expensing subsequent expenditure does not affect the measurement of biological assets nor does it have any effect on profit or loss; however, it affects the presentation of amounts in the statement of profit or loss. The submitter suggests amending IAS 41 to either require entities to capitalise subsequent expenditure or, instead, require entities to recognise it as an expense. The submitter says this would (a) reduce diversity in practice, and (b) assist users of financial statements when comparing the performance of entities. The submitter says stakeholders in its jurisdiction (including lenders, investors and regulators) have reported difficulties in understanding and comparing components of profit or loss reported in the financial statements of entities with biological assets.

Require capitalisation or, instead, require recognition as an expense

31. Although a requirement to expense all subsequent expenditure would be simple to understand and apply, we note that IAS 40 *Investment Property* requires an entity to capitalise subsequent expenditure for investment property measured at fair value. Paragraph B40 of the Basis for Conclusions on IAS 40 explains the reason for this requirement (emphasis added):

> Some believe that there is no need to capitalise subsequent expenditure in a fair value model and that all subsequent expenditure should be recognised as an expense. However, others believe—and the Board agreed—that the *failure to capitalise subsequent expenditure would lead to a distortion of the reported components of financial performance*. Therefore, the Standard requires that an entity should determine whether subsequent expenditure should be capitalised using a test similar to the test used for owner-occupied property in IAS 16.

32. We also think users of financial statements might find it more useful if entities were to capitalise subsequent expenditure, rather than expense it. For example, paragraph 4.3.1 of the CSA Staff Notice states (emphasis added):

> …Issuers who expense biological asset costs as incurred should consider whether this accounting policy results in information that is relevant to the decision-making needs of investors. These issuers are encouraged to *provide supplemental information in their MD&A such as, for example, information about the impact that capitalization of direct and indirect costs related to biological assets would have had on the P&L*. This type of information may be useful to investors who want to compare gross profit between different issuers.

33. In addition, outreach responses and our additional research (see paragraphs 11–20 above) identified that for some industry sectors such as fish farming, entities generally capitalise subsequent expenditure. They do so to better reflect that most of the change in fair value comes from growth (as a result of expenditure on feed and medicine), and not simply from price changes.

34. Accordingly, we think it is likely that any such amendment to IAS 41 to address this matter would need to require entities to capitalise subsequent expenditure, rather than recognise it as an expense. However, if the Board or Committee were to develop an amendment that requires capitalisation of subsequent expenditure, we think significant time and effort (of both the Board/Committee and stakeholders) would be needed to research, for example:

    (a) information needs of investors across the diverse range of biological assets[1];

    (b) whether all subsequent expenditure should be capitalised or only expenditure that meets particular criteria;

    (c) if only some subsequent expenditure should be capitalised, what the criteria should be;

    (d) whether any criteria developed would work across the diverse range of biological assets; and

    (e) whether it is feasible for entities to analyse subsequent expenditure for all biological assets and separately identify those that meet the criteria for capitalisation. For example, in deciding not to specify requirements for subsequent expenditure in IAS 41, the IASC Board observed in paragraph B62 of IAS 41 that '…some also argue that it would sometimes be difficult to prescribe which costs should be recognised as expenses and which costs should be capitalised; for example, in the case of vet fees paid for delivering a calf…'. One outreach respondent also noted that it might be challenging for entities with some types of biological assets to determine an appropriate allocation of expenses and that any such allocation might be arbitrary.

[1] Paragraph 6 of IAS 41 states: 'Agricultural activity covers a diverse range of activities; for example, raising livestock, forestry, annual or perineal cropping, cultivating orchards and plantations, floriculture and aquaculture (including fish farming)…'

Would requiring capitalisation result in benefits for financial statement users?

35. We have little evidence at this stage to suggest that requiring the capitalisation of subsequent expenditure would solve an identified concern in financial reporting. Based on the CSA Staff Notice, it would appear that at least some investors have a different financial reporting concern. Paragraphs 4.1 and 4.3.1 of the CSA Staff Notice state in relation to entities that are in the business of producing cannabis (emphasis added):

> 4.1 …It is critical for investors to be able to understand how much it costs a company to produce its product. Since fair value amounts in the P&L of [a cannabis producer] are not costs that have been incurred related to cannabis sold, it is important for all fair value amounts to be separately disclosed, so that *investors can understand a company's cost of sales excluding any fair value amounts*…
>
> 4.3.1 When issuers elect to expense direct and indirect costs related to biological assets, the P&L will typically include costs incurred in the current period related to cannabis which has not yet been sold. As a result, *investors may not be able to determine which costs relate to cannabis sold in the period*. Issuers in other industries (e.g. manufacturing) that are within the scope of IAS 2 [*Inventories*], but that do not have biological assets, will generally provide this information because IAS 2 requires the capitalization of costs which are directly and indirectly related to the production of inventories. *Investors in the cannabis industry may want information about the cost of cannabis sold in the period, regardless of whether an issuer elects to capitalize or expense* biological asset costs under IAS 41…

36. Informal discussions with some stakeholders in Canada confirmed the summary in the CSA Staff Notice. We understand that cannabis producers distinguish themselves based on the cost of production—cost is one of their key performance indicators. Consequently, investors in that industry are interested in understanding the cumulative

cost of producing cannabis sold in any given period; they generally view the production and sale of cannabis to be more akin to the production and sale of inventory (accounted for applying IAS 2), rather than as biological assets.

37. We note that requiring entities to capitalise or expense subsequent expenditure would not, in itself, provide investors with information about the cumulative cost of biological assets sold during a period. Determining that cumulative cost would require tracking of either (a) the cumulative cost of each biological asset over its life until sale; or (b) the cumulative fair value changes recognised for each biological asset over its life until sale. IAS 41 does not currently require an entity to separately track either of these amounts.

38. To illustrate, we have used the example in paragraphs 9–10 above and assumed that Entity X incurs subsequent expenditure of CU150 in 2019 and sells the biological asset at its FV of CU750 at 30 June 2019. For simplicity, we have also assumed that Entity X purchased the biological asset in 2017 for CU200 (there were no changes in FV in 2017). This means that, in summary, at the time of sale the FV of the biological asset is CU750, comprising cumulative expenditure of CU650 and cumulative change in FV of CU100.

39. The following table illustrates the information we understand investors in the cannabis industry would like to receive when cannabis is sold and compares it with the information they would receive if Entity X were to capitalise subsequent expenditure.

	Investor information request (CU)	**Capitalisation of subsequent expenditure (CU)**
Revenue	750	750
Cost of goods sold	(650)[2]	(750)[3]
Gross profit	**100**	**0**
Cumulative change in FV	(100)[4]	0
Effect on profit or loss	**0**	**0**

40. Accordingly, we think requiring entities to capitalise subsequent expenditure may not meet investor needs for at least some types of biological assets. Providing information about the cumulative cost of biological assets sold during a period would go beyond simply requiring entities to either capitalise or expense subsequent expenditure. Instead, it would require a more fundamental consideration of the measurement model in IAS 41 for at least some biological assets.

41. We understand that the production cycle for cannabis is relatively short (14-18 weeks) and that subsequent expenditure is relatively high. It may be that cumulative cost information is particularly useful only for some biological assets with a short harvesting period, and for which subsequent expenditure is significant. However, in our view any project that might address cumulative cost information would be a standard-setting project for the Board—this is because it would involve consideration of the fair value measurement model in IAS 41, even if only for a narrow population of biological assets. Such a project would be more in the nature of the Bearer Plants project that resulted in amendments to IAS 16 and IAS 41 in 2014.

[2] Calculated as purchase price of CU200 plus subsequent expenditure of CU300 in 2018 and CU150 in 2019.

[3] FV of biological asset at date of sale.

[4] Increase in FV of CU100 over the life of the biological asset, recognised in profit or loss in 2018 when the change in FV occurred.

42. We understand that the matter could become more widespread because of changes to the licensing of cannabis being made or contemplated in various jurisdictions. If that is the case, we think it is something the Board could consider based on feedback to its next Agenda Consultation regarding its priorities.

Other considerations

43. As explained in paragraph 7 of this paper, capitalising or expensing subsequent expenditure does not affect the measurement of biological assets nor does it have any effect on profit or loss; however it affects the presentation of amounts in the statement of profit or loss.

44. The Board has a project on its standard-setting agenda on primary financial statements (PFS). As part of that project, the Board is developing improvements to the structure and content of the primary financial statements, with a focus on the statement of financial performance. The Board expects to publish an exposure draft before the end of 2019. Although the PFS project does not directly address whether an entity with biological assets capitalises or expenses subsequent expenditure, any amendments resulting from the PFS project would also be relevant for entities with biological assets.

Staff Conclusion

45. Based on our analysis, we recommend not adding a standard-setting project to the Committee's standard-setting agenda. This is because:

    (a) we have insufficient evidence to suggest that amending IAS 41 to require entities to capitalise subsequent expenditure (or, instead, requiring them to expense it) would result in an improvement to financial reporting that would justify the costs; and

    (b) amending IAS 41 to provide financial statement users with information about the cost of biological assets sold in a particular period would require a fundamental consideration of IAS 41 for at least some biological assets.

46. Instead, we recommend that the Committee publish a tentative agenda decision that:

    (a) confirms entities can either capitalise or expense subsequent expenditure;

(b) directs entities to the disclosure requirements in paragraphs 117–124 of IAS 1; and

(c) explains that the Committee did not add the matter to its standard-setting agenda because it has insufficient evidence to suggest that any standard-setting would result in an improvement to financial reporting that would justify the costs. This, thereby, gives stakeholders with the opportunity to provide us with such evidence in their responses to the tentative agenda decision.

Staff recommendation

47. Based on our assessment of the Committee's agenda criteria, we recommend that the Committee does not add the matter to its standard-setting agenda, and instead publish a tentative agenda decision setting out the matters noted in paragraph 46 of this paper. Appendix A to this paper sets out the proposed wording of the tentative agenda decision.

Questions 2 and 3 for the Committee
2. Does the Committee agree with our recommendation not to add this matter to its standard-setting agenda? 3. Does the Committee have any comments on the proposed wording of the tentative agenda decision set out in Appendix A to this paper?

Appendix A—proposed wording of the tentative agenda decision

Subsequent expenditure on biological assets (IAS 41 *Agriculture*)

The Committee received a request about the accounting for costs relating to the biological transformation (subsequent expenditure) of biological assets measured at fair value less costs to sell applying IAS 41. The request asked whether an entity capitalises subsequent expenditure (ie adds it to the carrying amount of the asset) or, instead, recognises the subsequent expenditure as an expense when incurred or instead.

The Committee observed that capitalising subsequent expenditure or recognising it as an expense has no effect on the measurement of biological assets nor does it have any effect on profit or loss; however, it affects the presentation of amounts in the statement of profit or loss.

IAS 41 does not specify requirements on the accounting for subsequent expenditure. Paragraph B62 of the Basis for Conclusions on IAS 41 explains that '…the [IASC] Board decided not to explicitly prescribe the accounting for subsequent expenditure related to biological assets in the Standard, because it believes to do so is unnecessary with a fair value measurement approach.'

Accordingly, the Committee concluded that, applying IAS 41, an entity either capitalises subsequent expenditure or recognises it as an expense when incurred. Applying paragraph 13 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, an entity would apply its accounting policy for subsequent expenditure consistently to each group of biological assets. An entity would also disclose the selected accounting policy applying paragraphs 117–124 of IAS 1 *Presentation of Financial Statements* if that disclosure would assist users of financial statements in understanding how those transactions are reflected in reported financial performance.

In the light of its analysis, the Committee considered whether to add a project to its standard-setting agenda on the accounting for subsequent expenditure on biological assets. The Committee has not obtained evidence to suggest that standard-setting on this matter at this time would result in an improvement to financial reporting that would be sufficient to outweigh the costs. The Committee therefore [decided] not to add this matter to its standard-setting agenda.

Appendix B––submission

Dear sirs:

Re: IAS 41 Agriculture – Accounting for Subsequent Expenditure

We are enclosing our submission to the IFRS Interpretations Committee, which asks the Committee to recommend amending IAS 41 to the International Accounting Standards Board, to clarify the accounting for costs incurred related to the biological transformation (i.e., subsequent expenditure) of biological assets. Stakeholders in our jurisdiction, including lenders, investors and regulators, are reporting significant difficulties understanding and comparing the components of financial performance reported in the financial statements of agricultural producers.

We understand that paragraph B62 of the Basis for IASC's Conclusions on IAS 41 explains that the IASC Board decided not to explicitly prescribe the accounting for subsequent expenditure related to biological assets because it believed to do so was unnecessary with a fair value measurement approach.[1] However, we note that IAS 40 *Investment Property*, which is another standard with a fair value model, does provide guidance in this area. Paragraph B40 of the Basis for IASC's Conclusions on IAS 40 indicates that while some believe that there is no need to capitalize subsequent expenditure in a fair value model, others believe–and the IASC Board agreed–that failure to capitalize subsequent expenditure would lead to a distortion of the reported components of financial performance. Given both standards were developed around the same time, we believe that the need for guidance on accounting for subsequent expenditure existed at the time IAS 41 was issued, and the concerns raised by our stakeholders highlight that this need continues to exist.

Our IFRS Discussion Group (Group) discussed this issue at its June 21, 2018 meeting, given the media has been reporting user concerns with assessing the financial performance of agricultural producers in our jurisdiction that apply IAS 41, notably publicly traded licensed

[1] We understand that the IASC Board considered respondents' comments to its exposure draft in July 1999. The exposure draft included a proposal that costs of producing and harvesting biological assets should be charged to expense when incurred. Paragraph B62 of the Basis for IASC's Conclusions indicated some believed that there was no need to capitalize subsequent expenditure in a fair value model, and some also argued that it would be difficult to prescribe which costs should be recognized as expenses and which costs should be capitalized. The IASC Board decided not to explicitly prescribe the accounting for subsequent expenditure related to biological assets.

producers in the rapidly expanding cannabis industry. With the legalization of cannabis for recreational use in Canada, there is an increased amount of investor capital flowing into the industry. Because IAS 41 does not explicitly prescribe the accounting for subsequent expenditure related to biological assets, Canadian entities either capitalize or expense subsequent expenditure, and many have not disclosed this as an accounting policy choice.

Our staff also reviewed the financial statements of a sample of entities operating in countries such as Brazil, Indonesia, Malaysia, New Zealand, Norway, Poland, Russia and United Kingdom, and in industries such as palm oil, crops, hogs, poultry, beef cattle and aquaculture. The sampled financial statements showed that there was not a consistent approach to either capitalizing or expensing subsequent expenditure. This inconsistent approach indicates that diversity also exists outside Canada and in industries beyond cannabis.

We are also aware of a large, dual-listed licensed producer reporting under IFRS Standards that amended its accounting policy note for biological assets in the same year it was listed in the United States. The entity first amended its policy note to indicate that it capitalizes the direct and indirect costs (except for depreciation) incurred related to biological transformation before measuring the biological assets at fair value less costs to sell. As a result, certain comparative amounts have been reclassified to conform to the current presentation, including amounts in its Statement of Comprehensive Income. The entity subsequently changed its accounting policy and further amended its policy note to indicate it capitalizes all the direct and indirect costs, including labour related costs, grow consumables, materials, utilities, facilities costs, quality and testing costs, and production related depreciation. The entity explained that the revised policy and presentation would provide more relevant financial information to users.

We note that applying either a capitalization or expense approach will affect how information is reported in the Statement of Comprehensive Income, particularly whether the amount presented as the change in fair value less costs to sell includes subsequent expenditure related to biological transformation. Since IAS 41 only requires such change to be included in profit or loss and is silent on the treatment at the gross profit level, multiple approaches are used to report components of financial performance. As a result, users are finding it difficult to understand how key measures of income and expense such as gross profit and cost of goods sold are determined. To respond to users’ concerns, our securities regulators published guidance on disclosure expectations for licensed producers in the cannabis industry to ensure transparent information about the entities' financial performance is provided. For example, entities that expense costs related to biological assets as incurred are expected to provide supplemental information about the impact that capitalization of such costs would have had on the components of the Statement of Comprehensive Income.

Based on the points noted in this letter, we believe that IAS 41 is unclear in accounting for subsequent expenditure compared to other IFRS Standards with a fair value model. This ambiguity has led to significant complexities for users in understanding the reported components of financial performance and has drawn media attention given the effects on investing and lending decisions in our capital markets. Therefore, we think that IAS 41 should be amended to require a single approach to accounting for subsequent expenditure to reduce presentation diversity in the Statement of Comprehensive Income and, aid in the assessment of performance and comparability between entities.

The Appendix to this letter outlines a fact pattern and the different views that our Group considered for this issue.

Appendix to the submission

Issue

IAS 41 Agriculture requires biological assets to be measured on initial recognition and at the end of each reporting period at fair value less costs to sell, except where fair value cannot be measured reliably.

Once a biological asset has been harvested, the costs incurred thereafter are within the scope of IAS 2 *Inventories*. However, the issue is how to account for the costs incurred related to the biological transformation (also referred to as "subsequent expenditure") of a biological asset between the point of initial recognition and the point of harvest. Should the subsequent expenditure related to a biological asset that is measured at fair value less costs to sell be expensed or capitalized?

Fact Pattern

An entity has cannabis plants measured at fair value less costs to sell (FVLCS) of $200 as at December 31, 2017, which is near the beginning of their growth cycle. During the first quarter of 2018, $300 of expenditure are incurred to grow the cannabis plants and the FVLCS of the cannabis plants at March 31, 2018 is $600.

Illustration

The accounting treatment of subsequent expenditure affects disclosures and expenditure classification in the Statement of Comprehensive Income. The figure below illustrates the fact pattern above and the effect under the two views (i.e., Views 1 and 2) noted below.

	View 1 Expense Subsequent Expenditure		View 2 Capitalize Subsequent Expenditure	
	Biological Asset Continuity Debit / (Credit)	Profit or Loss Impact Debit / (Credit)	Biological Asset Continuity Debit / (Credit)	Profit or Loss Impact Debit / (Credit)
FVLCS, December 31, 2017	**CU200**		**CU200**	
Capitalized to biological assets			CU300	
Expensed		CU300		
Change in FVLCS on growing cannabis	CU400	(CU400)	CU100	(CU100)
FVLCS, March 31, 2018	**CU600**		**CU600**	
Net Profit or Loss impact		**(CU100)**		**(CU100)**

Views and Discussions

View 1 – Expense subsequent expenditure.

Under this view, the remeasurement of FVLCS of cannabis plants up to the point of harvest is meant to capture the changes in value throughout the biological transformation of the cannabis plants in profit or loss.

By expensing subsequent expenditure, a financial statement user can see the change in FVLCS separate from the subsequent expenditure incurred to grow the biological asset (i.e., gross presentation).

View 2 – Capitalize subsequent expenditure.

Under this view, the amount shown as a change in FVLCS is net of subsequent expenditure incurred as those costs contributed to the growth of the cannabis plants, and therefore, the increase in FVLCS.

This approach would result in the change in FVLCS of the growing cannabis being attributed purely to the natural growth of the plants.

View 3 – There is an accounting policy choice.

Under this view, paragraph B62 of the Basis for IASC's Conclusions on IAS 41 is taken into consideration. This paragraph notes that "the Board decided not to explicitly prescribe the accounting for subsequent expenditure related to biological assets in the Standard, because it believes to do so is unnecessary with a fair value measurement approach."

Based on the above, an entity could develop an accounting policy choice with reference to guidance in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, which requires, among other things, that management use its judgment in developing and applying an accounting policy that results in information that is relevant and reliable.

Reasons for the IFRS Interpretations Committee to address this issue

We have assessed this issue against the Interpretations Committee's agenda criteria:

Criteria	**Assessment**
1. Is the issue widespread and has, or is expected to have, a material effect on those affected?	In Canada, users find it challenging to understand and compare the financial performance of agricultural producers, specifically in the cannabis industry because of the different approaches in accounting for subsequent expenditure related to biological assets that are used in practice. Based on a sample of entities reviewed, we also observe this diversity in practice at a

	global level whereby subsequent expenditure related to biological assets is either capitalized or expensed.
2. Would financial reporting be improved through the elimination, or reduction, of diverse reporting methods?	We think that by resolving the ambiguity in IAS 41 as to the approach in accounting for subsequent expenditure related to biological assets, diversity in practice would be eliminated. As a result, financial reporting would be improved because entities would apply IAS 41 consistently, and therefore, would improve users' understanding of the financial results.
3. Can the issue be resolved efficiently within the confines of IFRS Standards and the *Conceptual Framework for Financial Reporting*?	We think that this issue can be resolved efficiently by amending the requirements in IAS 41.
4. Is the issue sufficiently narrow in scope that the Interpretations Committee can address this issue in an efficient manner, but not so narrow that it is not cost-effective for the Interpretations Committee to undertake the due process that would be required when making changes to IFRS Standards?	We think that this issue is sufficiently narrow in scope because it relates to the specific application of IAS 41.
5. Will the solution developed by the Interpretations Committee be effective for a reasonable time period? The Interpretations Committee will not add an item to its agenda if the issue is being addressed in a forthcoming Standard and/or if a short-term improvement is not justified.	We think that the solution will be effective for a reasonable period for agricultural producers because there is currently no IASB project proposing changes to this Standard.