

2014

IFRS Foundation: Framework-based IFRS Teaching Material

Stage 3– the IAS 8 hierarchy: the Amalgam case study



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Amalgam case study

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This material has benefited greatly from the feedback and comments from people attending a series of workshops on the Framework-based approach to teaching International Financial Reporting Standards (IFRS) organised by the IFRS Foundation and others and from peer review by a number of anonymous reviewers.

Background

Amalgam has been listed on the Afriganistan Stock Exchange for more than ten years.¹ It was founded by Mrs Conglomerate (Mrs C) and she holds the controlling (80 per cent) equity interest. Amalgam's functional currency is the US dollar (\$).

For many years Mr Judgement (Mr J) has led the financial reporting team at Amalgam. Last year, Amalgam's financial statements were prepared in accordance with IFRS for the first time. Previously, the financial reporting requirements applied were mostly tax-based. Mr J found that he needed to exercise a greater amount of judgement and needed to make many more estimates in order to apply IFRS.

In the current reporting period (20X2) Amalgam enters into a number of transactions for which Mr J cannot find specific IFRS requirements. Mr J wonders how, in the absence of explicit IFRS requirements, he should account for and report those transactions in Amalgam's financial statements for the year ended 31 December 20X2. Consequently, he seeks your expert opinion on how to account for the following economic phenomena (for example, a transaction or other event) in accordance with IFRS.

Mushroom farming

On 1 February 20X2 Amalgam acquires a mushroom farming business. When visiting the mushroom farming operation, Mr J is surprised to learn that mushrooms are neither plants nor animals—they are fungi. On returning to his office Mr J inspects the definition of a biological asset in IAS 41 *Agriculture* and is surprised to find that definition to be limited to living animals and living plants. Furthermore, he cannot find where in IFRS it is specified how to account for the fungi that Amalgam is farming (ie the living mushrooms).

¹ The names of individuals, entities and places in this case study are fictitious. Any resemblance to actual people, entities or places is purely coincidental.

Reorganisation

On 31 December 20X2 Amalgam acquires all the equity of Ation from Conglomerate in exchange for \$20,000 million in cash. Mrs C owns all the equity of Conglomerate and controls both Conglomerate and Amalgam.

Summary financial information for Amalgam and Ation on 31 December 20X2 (immediately before the transaction above) is as follows:

	Amalgam		Ation	
	<i>Carrying amount</i>	<i>Fair value</i>	<i>Carrying amount</i>	<i>Fair value</i>
	<i>\$'millions</i>	<i>\$'millions</i>	<i>\$'millions</i>	<i>\$'millions</i>
Identifiable assets	300,000	600,000	35,000	50,000
Liabilities	(200,000)	(190,000)	(32,000)	(29,000)
Contingent liabilities	–	(10,000)	–	(3,000)
	100,000	400,000	3,000	18,000

Gold acquired and held as a 'store of wealth'

On 30 June 20X2 Amalgam acquires 1,000,000 ounces of gold at \$1,000 per ounce and stores it in a secure vault at the local branch of an international bank. Amalgam neither trades in gold nor does it have any use for the gold, other than as a 'store of wealth'. Amalgam's risk management team expect to hold the gold for the foreseeable future and the cash used to pay for the gold is surplus to the entity's foreseeable cash flow needs.

At 31 December 20X2 (the end of the current annual reporting period) gold is trading at \$1,500 per ounce and Amalgam continues to hold 1,000,000 ounces of gold as a store of wealth.

Artwork collection

In September 20X2 Amalgam begins collecting artworks for the first time. It acquires 10 paintings at auctions in London, Hong Kong and New York at a total cost of \$1,000 million.

Amalgam neither trades in artworks nor does it intend to do so in the future. However, in managing the art collection, it is envisaged that some artworks might need to be sold to fund the acquisition of other, more desirable pieces.

The artwork collection is stored in a purpose-built underground vault at Amalgam's head office building. On occasion, Amalgam might invite its most important customers and other special guests to view the collection at no charge.

Amalgam's risk management team expect to hold the art indefinitely and the cash used to pay for the collection is surplus to the entity's foreseeable cash flow needs.

<i>Some IFRS issues for class discussion</i>
In the absence of an IFRS that specifically applies to a transaction or other event, how does an entity develop an accounting policy for that transaction or other event?
How would you advise Mr J when he is developing an accounting policy for Amalgam to account for the growing mushrooms?
How would you advise Mr J when he is developing an accounting policy for the acquisition of Aton in Amalgam's consolidated financial statements?
How would you advise Mr J when he is developing an accounting policy for Amalgam to account for the gold held as a store of wealth?
How would you advise Mr J when he is developing an accounting policy for Amalgam to account for the artworks held as a store of wealth?