

Effective for annual periods  
beginning on or after 1 January 2009\*

*Hong Kong Accounting Standard 23 (Revised)*

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## Borrowing Costs

\* (a) HKSA 23 (Revised) is applicable for annual periods beginning on or after 1 January 2009. Earlier application is permitted. HKAS 23 (Revised) supersedes HKAS 23 issued in 2004.

(b) [An entity shall apply amendments resulting from \*Improvements to HKFRSs\* issued in October 2008 for annual periods beginning on or after 1 January 2009.](#)



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香港會計師公會

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## BORROWING COSTS

Hong Kong Accounting Standard 23 *Borrowing Costs* (HKAS 23) is set out in paragraphs 1 – 30. All of the paragraphs have equal authority. HKAS 23 should be read in the context of its core principle and the Basis for Conclusions, the *Preface to Hong Kong Financial Reporting Standards* and the *Framework for the Preparation and Presentation of Financial Statements*. HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

This revised Standard was issued in June 2007. It supersedes HKAS 23, issued in 2004.

## Hong Kong Accounting Standard 23 *Borrowing Costs*

### Core principle

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- 1 **Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset form part of the cost of that asset. Other borrowing costs are recognised as an expense.**

### Scope

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- 2 **An entity shall apply this Standard in accounting for borrowing costs.**
- 3 The Standard does not deal with the actual or imputed cost of equity, including preferred capital not classified as a liability.
- 4 An entity is not required to apply the Standard to borrowing costs directly attributable to the acquisition, construction or production of:
- (a) a qualifying asset measured at fair value, for example a biological asset; or
  - (b) inventories that are manufactured, or otherwise produced, in large quantities on a repetitive basis.

### Definitions

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- 5 **This Standard uses the following terms with the meanings specified:**
- Borrowing costs* are interest and other costs that an entity incurs in connection with the borrowing of funds.**
- A qualifying asset* is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.**
- 6 Borrowing costs may include:
- (a) interest on bank overdrafts and short-term and long-term borrowings;
  - (b) amortisation of discounts or premiums relating to borrowings;
  - (c) amortisation of ancillary costs incurred in connection with the arrangement of borrowings;
  - (d) finance charges in respect of finance leases recognised in accordance with HKAS 17 *Leases*; and
  - (e) exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs.
- 7 Depending on the circumstances, any of the following may be qualifying assets:
- (a) inventories
  - (b) manufacturing plants

- (c) power generation facilities
- (d) intangible assets
- (e) investment properties.

Financial assets, and inventories that are manufactured, or otherwise produced, over a short period of time, are not qualifying assets. Assets that are ready for their intended use or sale when acquired are not qualifying assets.

## Recognition

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- 8 An entity shall capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. An entity shall recognise other borrowing costs as an expense in the period in which it incurs them.**
- 9 Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are included in the cost of that asset. Such borrowing costs are capitalised as part of the cost of the asset when it is probable that they will result in future economic benefits to the entity and the costs can be measured reliably. When an entity applies HKAS 29 *Financial Reporting in Hyperinflationary Economies*, it recognises as an expense the part of borrowing costs that compensates for inflation during the same period in accordance with paragraph 21 of that Standard.

### Borrowing costs eligible for capitalisation

- 10 The borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are those borrowing costs that would have been avoided if the expenditure on the qualifying asset had not been made. When an entity borrows funds specifically for the purpose of obtaining a particular qualifying asset, the borrowing costs that directly relate to that qualifying asset can be readily identified.
- 11 It may be difficult to identify a direct relationship between particular borrowings and a qualifying asset and to determine the borrowings that could otherwise have been avoided. Such a difficulty occurs, for example, when the financing activity of an entity is co-ordinated centrally. Difficulties also arise when a group uses a range of debt instruments to borrow funds at varying rates of interest, and lends those funds on various bases to other entities in the group. Other complications arise through the use of loans denominated in or linked to foreign currencies, when the group operates in highly inflationary economies, and from fluctuations in exchange rates. As a result, the determination of the amount of borrowing costs that are directly attributable to the acquisition of a qualifying asset is difficult and the exercise of judgement is required.
- 12 To the extent that an entity borrows funds specifically for the purpose of obtaining a qualifying asset, the entity shall determine the amount of borrowing costs eligible for capitalisation as the actual borrowing costs incurred on that borrowing during the period less any investment income on the temporary investment of those borrowings.**
- 13 The financing arrangements for a qualifying asset may result in an entity obtaining borrowed funds and incurring associated borrowing costs before some or all of the funds are used for expenditures on the qualifying asset. In such circumstances, the funds are often temporarily invested pending their expenditure on the qualifying asset. In determining the amount of borrowing costs eligible for capitalisation during a period, any investment income earned on such funds is deducted from the borrowing costs incurred.

14. **To the extent that an entity borrows funds generally and uses them for the purpose of obtaining a qualifying asset, the entity shall determine the amount of borrowing costs eligible for capitalisation by applying a capitalisation rate to the expenditures on that asset. The capitalisation rate shall be the weighted average of the borrowing costs applicable to the borrowings of the entity that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs that an entity capitalises during a period shall not exceed the amount of borrowing costs it incurred during that period.**
- 15 In some circumstances, it is appropriate to include all borrowings of the parent and its subsidiaries when computing a weighted average of the borrowing costs; in other circumstances, it is appropriate for each subsidiary to use a weighted average of the borrowing costs applicable to its own borrowings.

**Excess of the carrying amount of the qualifying asset over recoverable amount**

- 16 When the carrying amount or the expected ultimate cost of the qualifying asset exceeds its recoverable amount or net realisable value, the carrying amount is written down or written off in accordance with the requirements of other Standards. In certain circumstances, the amount of the write-down or write-off is written back in accordance with those other Standards.

**Commencement of capitalisation**

- 17 **An entity shall begin capitalising borrowing costs as part of the cost of a qualifying asset on the commencement date. The commencement date for capitalisation is the date when the entity first meets all of the following conditions:**
- (a) **it incurs expenditures for the asset;**
  - (b) **it incurs borrowing costs; and**
  - (c) **it undertakes activities that are necessary to prepare the asset for its intended use or sale.**
- 18 Expenditures on a qualifying asset include only those expenditures that have resulted in payments of cash, transfers of other assets or the assumption of interest-bearing liabilities. Expenditures are reduced by any progress payments received and grants received in connection with the asset (see HKAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*). The average carrying amount of the asset during a period, including borrowing costs previously capitalised, is normally a reasonable approximation of the expenditures to which the capitalisation rate is applied in that period.
- 19 The activities necessary to prepare the asset for its intended use or sale encompass more than the physical construction of the asset. They include technical and administrative work prior to the commencement of physical construction, such as the activities associated with obtaining permits prior to the commencement of the physical construction. However, such activities exclude the holding of an asset when no production or development that changes the asset's condition is taking place. For example, borrowing costs incurred while land is under development are capitalised during the period in which activities related to the development are being undertaken. However, borrowing costs incurred while land

acquired for building purposes is held without any associated development activity do not qualify for capitalisation.

### **Suspension of capitalisation**

- 20 An entity shall suspend capitalisation of borrowing costs during extended periods in which it suspends active development of a qualifying asset.**
- 21 An entity may incur borrowing costs during an extended period in which it suspends the activities necessary to prepare an asset for its intended use or sale. Such costs are costs of holding partially completed assets and do not qualify for capitalisation. However, an entity does not normally suspend capitalising borrowing costs during a period when it carries out substantial technical and administrative work. An entity also does not suspend capitalising borrowing costs when a temporary delay is a necessary part of the process of getting an asset ready for its intended use or sale. For example, capitalisation continues during the extended period that high water levels delay construction of a bridge, if such high water levels are common during the construction period in the geographical region involved.

### **Cessation of capitalisation**

- 22 An entity shall cease capitalising borrowing costs when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.**
- 23 An asset is normally ready for its intended use or sale when the physical construction of the asset is complete even though routine administrative work might still continue. If minor modifications, such as the decoration of a property to the purchaser's or user's specification, are all that are outstanding, this indicates that substantially all the activities are complete.
- 24 When an entity completes the construction of a qualifying asset in parts and each part is capable of being used while construction continues on other parts, the entity shall cease capitalising borrowing costs when it completes substantially all the activities necessary to prepare that part for its intended use or sale.**
- 25 A business park comprising several buildings, each of which can be used individually, is an example of a qualifying asset for which each part is capable of being usable while construction continues on other parts. An example of a qualifying asset that needs to be complete before any part can be used is an industrial plant involving several processes which are carried out in sequence at different parts of the plant within the same site, such as a steel mill.

### **Disclosure**

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- 26 An entity shall disclose:**
- (a) the amount of borrowing costs capitalised during the period; and**
  - (b) the capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation.**

### **Transitional provisions**

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- 27 When application of this Standard constitutes a change in accounting policy, an entity shall apply the Standard to borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after the effective date.
- 28 However, an entity may designate any date before the effective date and apply the Standard to borrowing costs relating to all qualifying assets for which the commencement date for capitalisation is on or after that date.

### **Effective date**

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- 29 An entity shall apply the Standard for annual periods beginning on or after 1 January 2009. Earlier application is permitted. If an entity applies the Standard from a date before 1 January 2009, it shall disclose that fact.

### **Withdrawal of HKAS 23 (issued 2004)**

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- 30 This Standard supersedes HKAS 23 *Borrowing Costs* issued in 2004.

## Appendix Amendments to other pronouncements

The amendments in this appendix shall be applied for annual periods beginning on or after 1 January 2009. If an entity applies this Standard for an earlier period, the amendments in this appendix shall be applied for that earlier period. In the amended paragraphs, new text is underlined and deleted text is struck through.

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The amendments contained in this appendix when this Standard was issued have been incorporated into the relevant Standards.

A1 ~~HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards* is amended as described below.~~

~~In the rubric, the first sentence is amended as follows:~~

~~Hong Kong Financial Reporting Standard 1 *First-time Adoption of Hong Kong Financial Reporting Standards* (HKFRS 1) is set out in paragraphs 1–47F 1-47G.~~

~~Paragraphs 9, 12 and 13 are amended, after paragraph 25H a heading and paragraph 25I are inserted, and paragraph 47G is added as follows:~~

9 ~~The transitional provisions in other HKFRSs apply to changes in accounting policies made by an entity that already uses HKFRSs; they do not apply to a *first-time adopter's* transition to HKFRSs, except as specified in paragraphs 25D, 25H, 25I, 34A and 34B.~~

12 ~~This HKFRS establishes two categories of exceptions to the principle that an entity's opening HKFRS balance sheet shall comply with each HKFRS:~~

(a) ~~paragraphs 13-25H and 36A-36C grant exemptions from some requirements of other HKFRSs.~~

(b) ~~paragraphs 26-34B prohibit retrospective application of some aspects of other HKFRSs.~~

13 ~~An entity may elect to use one or more of the following exemptions:~~

(a) ~~...~~

(l) ~~fair value measurement of financial assets or financial liabilities at initial recognition (paragraph 25G); and~~

(m) ~~a financial asset or an intangible asset accounted for in accordance with HK(IFRIC)-Int 12 *Service Concession Arrangements* (paragraph 25H); and~~

(n) ~~borrowing costs (paragraph 25I).~~

~~An entity shall not apply these exemptions by analogy to other items.~~

### **Borrowing costs**

25I ~~A first-time adopter may apply the transitional provisions set out in paragraphs 27 and 28 of HKAS 23 *Borrowing Costs*, as revised in 2007. In those paragraphs~~

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~~references to the effective date shall be interpreted as 1 January 2009 or the date of transition to HKFRSs, whichever is later.~~

~~47G An entity shall apply the amendments in paragraphs 13(n) and 25I for annual periods beginning on or after 1 January 2009. If an entity applies HKAS 23 for an earlier period, these amendments shall be applied for that earlier period.~~

~~A2 In HKAS 1 *Presentation of Financial Statements* the last sentence of paragraph 110 is deleted.~~

~~A3 In HKAS 7 *Cash Flow Statements* paragraph 32 is amended as follows:~~

~~32 The total amount of interest paid during a period is disclosed in the cash flow statement whether it has been recognised as an expense in the income statement or capitalised in accordance with the allowed alternative treatment in HKAS 23 *Borrowing Costs*.~~

~~A4 In HKAS 11 *Construction Contracts* the last sentence of paragraph 18 is amended as follows:~~

~~18 Costs that may be attributable to contract activity in general and can be allocated to specific contracts also include borrowing costs when the contractor adopts the allowed alternative treatment in HKAS 23 *Borrowing Costs*.~~

~~A5 In HKAS 16 *Property, Plant and Equipment* paragraph 23 is amended as follows:~~

~~23 The cost of an item of property, plant and equipment is the cash price equivalent at the recognition date. If payment is deferred beyond normal credit terms, the difference between the cash price equivalent and the total payment is recognised as interest over the period of credit unless such interest is recognised in the carrying amount of the item capitalised in accordance with the allowed alternative treatment in HKAS 23.~~

~~A6 In HKAS 38 *Intangible Assets* paragraph 32 is amended as follows:~~

~~32 If payment for an intangible asset is deferred beyond normal credit terms, its cost is the cash price equivalent. The difference between this amount and the total payments is recognised as interest expense over the period of credit unless it is capitalised in accordance with the capitalisation treatment permitted in HKAS 23 *Borrowing Costs*.~~

~~A7 In Hong Kong (IFRIC) Interpretation 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities* paragraph 8 is amended as follows:~~

~~8 The periodic unwinding of the discount shall be recognised in profit or loss as a finance cost as it occurs. The allowed alternative treatment of capitalisation under HKAS 23 is not permitted.~~

~~A8 In Hong Kong (IFRIC) Interpretation 12 *Service Concession Arrangements* paragraph 22 is amended as follows:~~

~~22 In accordance with HKAS 23, borrowing costs attributable to the arrangement shall be recognised as an expense in the period in which they are incurred unless the operator has a contractual right to receive an intangible asset (a right to charge users of the public service). In this case borrowing costs attributable to the arrangement may shall be capitalised during the construction phase of the arrangement in accordance with the allowed alternative treatment under that Standard.~~

## Basis for Conclusions on HKAS 23 *Borrowing Costs*

*This Basis for Conclusions accompanies, but is not part of, HKAS 23.*

HKAS 23 is based on IAS 23 *Borrowing Costs*. In approving HKAS 23, the Council of the Hong Kong Institute of Certified Public Accountants considered and agreed with the IASB's Basis for Conclusions on IAS 23. Accordingly, there are no significant differences between HKAS 23 and IAS 23. The IASB's Basis for Conclusions is reproduced below. The paragraph numbers of IAS 23 referred to below generally correspond with those in HKAS 23.

### Introduction

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- BC1 This Basis for Conclusions summarises the International Accounting Standards Board's considerations in reaching its conclusions on revising IAS 23 *Borrowing Costs* in 2007. Individual Board members gave greater weight to some factors than to others.
- BC2 The revisions to IAS 23 result from the Board's Short-term Convergence project. The project is being conducted jointly with the United States standard-setter, the Financial Accounting Standards Board (FASB). The objective of the project is to reduce differences between IFRSs and US generally accepted accounting principles (GAAP) that are capable of resolution in a relatively short time and can be addressed outside major projects. The revisions to IAS 23 are principally concerned with the elimination of one of the two treatments that exist for borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset. The application of only one method will enhance comparability. For the reasons set out below, the Board decided to eliminate the option of immediate recognition of such borrowing costs as an expense. It believes this will result in an improvement in financial reporting as well as achieving convergence in principle with US GAAP.
- BC3 The Board considered whether to seek convergence on the detailed requirements for the capitalisation of borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset. However, the Board noted statements by the US Securities and Exchange Commission (SEC) and the European Commission that the IASB and FASB should focus their short-term convergence effort on eliminating major differences of principle between IFRSs and US GAAP. For their purposes, convergence on the detailed aspects of accounting treatments is not necessary. The Board further noted that both IAS 23 and SFAS 34 *Capitalization of Interest Cost* were developed some years ago. Consequently, neither set of specific provisions may be regarded as being of a clearly higher quality than the other. Therefore, the Board concluded that it should not spend time and resources considering aspects of IAS 23 beyond the choice between capitalisation and immediate recognition as an expense. This Basis for Conclusions does not, therefore, discuss aspects of IAS 23 that the Board did not reconsider. Paragraphs BC19 – BC26 analyse the differences between IAS 23 and SFAS 34.

### Amendments to the scope

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#### Assets measured at fair value

- BC4 The exposure draft of proposed amendments to IAS 23 proposed excluding from the scope of IAS 23 assets measured at fair value. Some respondents objected to the proposal, interpreting the scope exclusion as limiting capitalisation of borrowing costs to qualifying assets measured at cost. The Board confirmed its decision not to require capitalisation of borrowing costs relating to assets that are measured at fair value. 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.

**Inventories that are manufactured, or otherwise produced, in large quantities on a repetitive basis**

- BC5 The US standard, SFAS 34, requires an entity to recognise as an expense interest costs for inventories that are routinely manufactured or otherwise produced in large quantities on a repetitive basis because, in the FASB's view, the informational benefit from capitalising interest costs does not justify the cost. The exposure draft did not make an exception for borrowing costs relating to such inventories. The exposure draft, therefore, proposed to require an entity to capitalise borrowing costs relating to inventories that are manufactured in large quantities on a repetitive basis and take a substantial period of time to get ready for sale. Respondents argued that capitalising those borrowing costs would create a significant administrative burden, would not be informative to users and would create a reconciling item between IFRSs and US GAAP.
- BC6 The Board decided to exclude from the scope of IAS 23 inventories that are manufactured, or otherwise produced, in large quantities on a repetitive basis, even if they take a substantial period of time to get ready for sale. The Board acknowledges the difficulty in both allocating borrowing costs to inventories that are manufactured in large quantities on a repetitive basis and monitoring those borrowing costs until the inventory is sold. It concluded that it should not require an entity to capitalise borrowing costs on such inventories because the costs of capitalisation are likely to exceed the potential benefits.

**Elimination of the option of immediate recognition as an expense of borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset**

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- BC7 The previous version of IAS 23 permitted two treatments for accounting for borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset. They could be capitalised or, alternatively, recognised immediately as an expense. SFAS 34 requires the capitalisation of such borrowing costs.
- BC8 The Board proposed in the exposure draft to eliminate the option of immediate recognition as an expense. Many respondents disagreed with the Board's proposal in the exposure draft, arguing that:
- (a) borrowing costs should not be the subject of a short-term convergence project.
  - (b) the Board had not explored in sufficient detail the merits of both accounting options.
  - (c) the proposal did not result in benefits for users of financial statements because:
    - (i) it addressed only one of the differences between IAS 23 and SFAS 34.
    - (ii) comparability would not be enhanced because the capital structure of an entity could affect the cost of an asset.

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- (iii) credit analysts reverse capitalised borrowing costs when calculating coverage ratios.
  - (d) the costs of implementing the capitalisation model in IAS 23 would be burdensome.
  - (e) the proposal was not consistent with the Board's approach on other projects (in particular, the second phase of the Business Combinations project).
- BC9 The Board concluded that borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are part of the cost of that asset. During the period when an asset is under development, the expenditures for the resources used must be financed. Financing has a cost. The cost of the asset should include all costs necessarily incurred to get the asset ready for its intended use or sale, including the cost incurred in financing the expenditures as a part of the asset's acquisition cost. The Board reasoned that recognising immediately as an expense borrowing costs relating to qualifying assets does not give a faithful representation of the cost of the asset.
- BC10 The Board confirmed that the objective of the project is not to achieve full convergence on all aspects of accounting for borrowing costs. Rather, it is to reduce differences between IFRSs and US GAAP that are capable of resolution in a relatively short time. The removal of a choice of accounting treatment and convergence in principle with US GAAP will enhance comparability. The Board acknowledges that capitalising borrowing costs does not achieve comparability between assets that are financed with borrowings and those financed with equity. However, it achieves comparability among all non-equity financed assets, which is an improvement.
- BC11 A requirement to recognise immediately as an expense borrowing costs relating to qualifying assets would not enhance comparability. Rather, comparability between assets that are internally developed and those acquired from third parties would be impaired. The purchase price of a completed asset purchased from a third party would include financing costs incurred by the third party during the development phase.
- BC12 Respondents to the exposure draft argued that requiring the capitalisation of borrowing costs is not consistent with the Board's proposal in the second phase of the Business Combinations project to require an entity to treat as an expense acquisition costs relating to a business combination. The Board disagrees with those respondents. Acquisition costs as defined in the context of a business combination are different from borrowing costs incurred in constructing or producing a qualifying asset. Borrowing costs are part of the cost necessarily incurred to get the asset ready for its intended use or sale. Acquisition costs relating to a business combination are costs incurred for services performed to help with the acquisition, such as due diligence and professional fees. They are not costs of assets acquired in a business combination.
- BC13 The Board concluded that the additional benefits in terms of higher comparability, improvements in financial reporting and achieving convergence in principle with US GAAP exceed any additional costs of implementation. Achieving convergence in principle with US GAAP on this topic is a milestone in the Memorandum of Understanding published by the FASB and IASB in February 2006, which is a step towards removal of the requirement imposed on foreign registrants with the SEC to reconcile their financial statements to US GAAP.
- BC14 The Board observes that there is an unavoidable cost of complying with any new financial reporting standard. Accordingly, the Board carefully considers the costs and benefits of any new pronouncement. In this case, the Board has not been told that preparers who elected to capitalise borrowing costs under the previous version of IAS 23 found doing so

unnecessarily burdensome. In the Board’s judgement, any additional costs of capitalising an item of cost of an asset are offset by the advantage of having all entities account for that item in the same way.

### **Effective date and transition**

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- BC15 Development of a qualifying asset may take a long time. Additionally, some assets currently in use may have undergone and completed their production or construction process many years ago. If the entity has been following the accounting policy of immediately recognising borrowing costs as an expense, the costs of gathering the information required to capitalise them retrospectively and to adjust the carrying amount of the asset may exceed the potential benefits. Hence, the Board decided to require prospective application, which was supported by respondents to the exposure draft.
- BC16 The Board noted that the revisions would result in information that is more comparable between entities. On that basis, if an entity wished to apply the revised Standard from any date before the effective date, users of the entity’s financial statements would receive more useful and comparable information than previously.
- BC17 Therefore, an entity is permitted to apply the revised Standard from any designated date before the effective date. However, if an entity applies the Standard from such an earlier date, it should apply the Standard to all qualifying assets for which the commencement date for capitalisation is on or after that designated date.
- BC18 The Board recognises that the Standard may require an entity that reconciles its IFRS financial statements to US GAAP to maintain two sets of capitalisation information—one set that complies with the requirements of IAS 23 and one that complies with the requirements of SFAS 34. The Board wishes to avoid imposing on such entities the need to maintain two sets of capitalisation information. Therefore, before the effective date, the Board will consider what actions it might take to avoid this outcome.

### **Differences between IAS 23 and SFAS 34**

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- BC19 The following paragraphs summarise the main differences between IAS 23 and SFAS 34.

#### **Definition of borrowing costs**

- BC20 IAS 23 uses the term “borrowing costs” whereas SFAS 34 uses the term “interest costs”. “Borrowing costs” reflects the broader definition in IAS 23, which encompasses interest and other costs, such as:
- (a) exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs; and
  - (b) amortisation of ancillary costs incurred in connection with the arrangement of borrowings.
- BC21 EITF Issue No. 99-9 concludes that derivative gains and losses (arising from the effective portion of a derivative instrument that qualifies as a fair value hedge) are part of the capitalised interest cost. IAS 23 does not address such derivative gains and losses.

## Definition of a qualifying asset

BC22 The main differences are as follows:

- (a) IAS 23 defines a qualifying asset as one that takes a substantial period of time to get ready for its intended use or sale. The SFAS 34 definition does not include the term *substantial*.
- (b) IAS 23 excludes from its scope qualifying assets that are measured at fair value. SFAS 34 does not address assets measured at fair value.
- (c) SFAS 34 includes as qualifying assets investments in investees accounted for using the equity method, in some circumstances.\* Such investments are not qualifying assets according to IAS 23.
- (d) SFAS 34 does not permit the capitalisation of interest costs on assets acquired with gifts or grants that are restricted by the donor or grantor in some situations. IAS 23 does not address such assets.

## Measurement

BC23 When an entity borrows funds specifically for the purpose of obtaining a qualifying asset:

- (a) IAS 23 requires an entity to capitalise the actual borrowing costs incurred on that borrowing. SFAS 34 states that an entity may use the rate of that borrowing.
- (b) IAS 23 requires an entity to deduct any income earned on the temporary investment of actual borrowings from the amount of borrowing costs to be capitalised. SFAS 34 does not generally permit this deduction, unless particular tax-exempt borrowings are involved.

BC24 SFAS 34 requires an entity to use judgement in determining the capitalisation rate to apply to the expenditures on the asset—an entity selects the borrowings that it considers appropriate to meet the objective of capitalising the interest costs incurred that otherwise could have been avoided. When an entity borrows funds generally and uses them to obtain a qualifying asset, IAS 23 permits some flexibility in determining the capitalisation rate, but requires an entity to use all outstanding borrowings other than those made specifically to obtain a qualifying asset.

## Disclosure requirements

BC25 IAS 23 requires disclosure of the capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation. SFAS 34 does not require this disclosure.

BC26 SFAS 34 requires disclosure of the total amount of interest cost incurred during the period, including the amount capitalised and the amount recognised as an expense. IAS 23 requires disclosure only of the amount of borrowing costs capitalised during the period. IAS 1 *Presentation of Financial Statements* requires the disclosure of finance costs for the period.

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\* While the investee has activities in progress necessary to commence its planned principal operations provided that the investee's activities include the use of funds to acquire qualifying assets for its operations.

**Consequential amendments to IAS 11 *Construction Contracts***

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BC27 IAS 11 paragraph 18 states that “costs that may be attributable to contract activity in general and can be allocated to specific contracts also include borrowing costs when the contractor adopts the allowed alternative treatment in IAS 23 *Borrowing Costs*.” The Board decided to delete the reference to IAS 23 in this paragraph because it is unnecessary. Attributing borrowing costs to contracts is not a matter of capitalisation. Rather, it is a matter of identifying the contract costs. The inclusion of borrowing costs in contract costs affects the presentation of borrowing costs in profit or loss. It does not affect the recognition of borrowing costs as specified in IAS 23.

## Dissenting opinions on IAS 23

### Dissent of Anthony T Cope, Philippe Danjou and Robert P Garnett

- DO1 The Board's decision to require the capitalisation of borrowing costs relating to qualifying assets will cause a significant change in accounting for the many preparers that currently apply the benchmark treatment of recognising borrowing costs as an expense. Messrs Cope, Danjou and Garnett believe that such a change will require the establishment of cumbersome measurement processes and monitoring of capitalised costs over a long period. This is likely to involve considerable accounting work and incremental auditing costs.
- DO2 Users of financial statements responding to the exposure draft did not support the change because they saw no informational benefit in a model that capitalises costs, other than the capitalisation of the actual economic cost of capital of the investment. In addition, Messrs Cope, Danjou and Garnett believe that a standard requiring the capitalisation of borrowing costs should discuss more extensively which assets qualify for the purpose of capitalising which borrowing costs.
- DO3 As a consequence, Messrs Cope, Danjou and Garnett dissent because, in their view, the costs of this particular change will far outweigh the benefits to users.
- DO4 In addition, this requirement to capitalise borrowing costs will achieve only limited convergence with US GAAP—differences will remain that could lead to materially different capitalised amounts. Furthermore, entities that are required to reconcile net income and shareholders' equity to US GAAP already have the option to capitalise borrowing costs and, thus, may recognise amounts that are more comparable to, albeit still potentially materially different from, those recognised in accordance with US GAAP.
- DO5 The Memorandum of Understanding published by the FASB and the IASB states that trying to eliminate differences between standards that are both in need of significant improvement is not the best use of resources. Messrs Cope, Danjou and Garnett support the convergence work programme, but only if it results in higher quality standards and improved financial reporting. They are of the opinion that IAS 23 and SFAS 34 are both in need of significant improvement and should not have been addressed as part of short-term convergence.

## Appendix

### Amendments to Basis for Conclusions on other pronouncements

*This appendix contains amendments to the Basis for Conclusions on other pronouncements that are necessary in order to ensure consistency with the revised IAS 23.*

\* \* \*

The amendments contained in this appendix when this *Basis for Conclusions* was issued have been incorporated into the relevant *Basis for Conclusions*.

~~BCA1 In the Basis for Conclusions on IFRS 1 *First-time Adoption of International Financial Reporting Standards*, after paragraph BC63D a heading and paragraph BC63E are added as follows:~~

#### ~~**Borrowing costs**~~

~~BC63E IAS 23 *Borrowing Costs* (as revised in 2007) contains transitional provisions because the Board acknowledged that if an entity has been following the accounting policy of immediately recognising borrowing costs as an expense and has not previously gathered the necessary information for capitalisation of borrowing costs, getting the information retrospectively may be costly. First-time adopters of IFRSs face problems similar to those facing entities that already apply IFRSs. Moreover, although first-time adopters have the option of using fair value as the deemed cost of an asset at the date of transition to IFRSs, this option is not applicable to all qualifying assets, such as inventories. Furthermore, the Board concluded that the existence of the deemed cost option is not sufficient to justify a more stringent requirement for the application of IAS 23 for first-time adopters than for entities that already apply IFRSs. A more stringent requirement for the adoption of the capitalisation treatment could be justified when IFRS 1 was originally issued because capitalisation was then an option. The requirements for the application of mandatory capitalisation, on the other hand, should be the same for entities that already apply IFRSs and for first-time adopters. Therefore, the Board decided to amend IFRS 1, allowing first-time adopters transitional provisions equivalent to those available to entities that already apply IFRSs in paragraphs 27 and 28 of IAS 23, as revised in 2007.~~

~~BCA2 In the Basis for Conclusions on IFRIC Interpretation 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*, the second sentence of paragraph BC26 is footnoted as follows:~~

~~In March 2007, IAS 23 was revised to require the previously allowed alternative treatment of capitalisation. Capitalisation of borrowing costs for a qualifying asset becomes the only accounting treatment. That revision does not affect the reasoning set out in this Basis for Conclusions.~~

~~BCA3 In the Basis for Conclusions on IFRIC Interpretation 12 *Service Concession Arrangements*, the first sentence of paragraph BC57, and paragraphs BC59 and BC77(f) are footnoted as follows:~~

~~In March 2007, IAS 23 was revised to require the previously allowed alternative treatment of capitalisation. Therefore, an entity is required to capitalise borrowing costs as part of the cost of a qualifying asset to the extent that they are directly attributable to its acquisition, construction or production until the asset is ready for its intended use or sale. That revision does not affect the reasoning set out in this Basis for Conclusions.~~

## Amendments to guidance on other pronouncements

The following amendments to guidance on other pronouncements are necessary in order to ensure consistency with the revised HKAS 23. In the amended paragraphs, new text is underlined and deleted text is struck through

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The amendments contained in this appendix when this Implementation Guidance was issued have been incorporated into the relevant Implementation Guidance.

~~IGA1— In the Guidance on Implementing HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards*, paragraphs IG23 and IG24 are amended as follows. Paragraph IG25 is deleted.~~

~~IG23— On first adopting HKFRSs, an entity adopts a policy of begins capitalising borrowing costs (HKAS 23 as revised in 2007) allowed alternative treatment) or not capitalising them (HKAS 23 benchmark treatment). The entity applies that policy consistently in its opening HKFRS balance sheet and in all periods presented in its first HKFRS financial statements. In accordance with paragraph 25I of the HKFRS, an entity:~~

~~(a) — capitalises borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009 or the date of transition to HKFRSs (whichever is later);~~

~~(b) — may elect to designate any date before 1 January 2009 or the date of transition to HKFRSs (whichever is later) and to capitalise borrowing costs relating to all qualifying assets for which the commencement date for capitalisation is on or after that date.~~

~~However, if the entity established a deemed cost for an asset, the entity does not capitalise borrowing costs incurred before the date of the measurement that established the deemed cost.~~

~~IG24— Under the allowed alternative treatment, HKAS 23 requires disclosure of interest capitalised during the period. Neither HKAS 23 nor the HKFRS requires disclosure of the cumulative amount capitalised.~~

~~IG25— [Deleted] HKAS 23 contains transitional provisions that encourage retrospective application, but permit an entity that adopts the allowed alternative treatment to capitalise (prospectively) only those borrowing costs incurred after the effective date of HKAS 23 that meet the criteria for capitalisation. However, if a first-time adopter adopts the HKAS 23 allowed alternative treatment, the HKFRS requires retrospective application of that treatment, even for periods before the effective date of HKAS 23 (paragraph 9 of the HKFRS).~~

~~IGA2— In the Guidance on Implementing HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, Example 2 is deleted.~~

~~IGA3— In the Illustrative Examples accompanying Hong Kong (IFRIC) Interpretation 12 *Service Concession Arrangements*, paragraphs IE15 and IE31 are amended as follows:~~

~~IE15— During the construction phase of the arrangement the operator's asset (representing its accumulating right to be paid for providing construction services) is classified as an intangible asset (licence to charge users of the infrastructure).~~

## BORROWING COSTS

The operator estimates the fair value of its consideration received to be equal to the forecast construction costs plus 5 per cent margin. It is also assumed that, in accordance with HKAS 23 *Borrowing Costs*, the operator adopts the allowed alternative treatment in HKAS 23 *Borrowing Costs* and therefore capitalises the borrowing costs, estimated at 6.7 per cent, during the construction phase of the arrangement:

IE31 During the construction phase of the arrangement the operator's asset (representing its accumulating right to be paid for providing construction services) is classified as a right to receive a licence to charge users of the infrastructure. The operator estimates the fair value of its consideration received or receivable as equal to the forecast construction costs plus 5 per cent. It is also assumed that, in accordance with HKAS 23 *Borrowing Costs*, the operator adopts the allowed alternative treatment in HKAS 23 *Borrowing Costs* and therefore capitalises the borrowing costs, estimated at 6.7 per cent, during the construction phase:

## Table of Concordance

This table shows how the contents of the superseded version of HKAS 23 and the revised version of HKAS 23 correspond. Paragraphs are treated as corresponding if they broadly address the same matter even though the guidance may differ.

<b>Superseded HKAS 23 paragraph</b>	<b>Revised HKAS 23 paragraph</b>	<b>Superseded HKAS 23 paragraph</b>	<b>Revised HKAS 23 paragraph</b>
Objective	1	18	15
1	2	19	16
2	None	20	17
3	3	21	18
4	5	22	19
5	6	23	20
6	7	24	21
7	None	25	22
8	None	26	23
9	None	27	24
10	8	28	25
11	None	29	26
12	9	30	None
13	10	31	None
14	11	None	4
15	12	None	27,28
16	13	None	29
17	14	None	30