IAS 23 *Borrowing Costs*

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SCOPE

Apply to: accounting for *borrowing costs.*

Borrowing costs = interest & other costs incurred in connection with borrowing of funds.
May include:

- Interest expense calculated using effective interest method (see IAS 39).
- Finance charges in respect of finance leases (see IAS 17).
- Exchange differences arising from foreign currency borrowings to extent that regarded as adjustment to interest costs (based on accounting policy).

Does NOT deal with: actual/imputed cost of equity, including preferred shares classified as equity.

NOT required to apply to: *borrowing costs directly attributable* to the acquisition, construction/ production of:

- A qualifying asset measured at FV (e.g., biological asset (within scope of IAS 41)).
- Inventories manufactured/otherwise produced, in large quantities on a repetitive basis.

RECOGNITION

- *Borrowing costs* that are *directly attributable* to acquisition/ construction/production of *qualifying asset* → capitalize as part of cost of that asset if:
  - Probable that will result in future economic benefits AND
  - Cost reliably measurable.
- Other *borrowing costs* → recognize as expense in period in which incurred.

Qualifying asset = asset that necessarily takes a substantial period of time to get ready for its intended use/sale.

- **Examples** of *qualifying assets* (depending on the circumstances) = inventories, manufacturing plants, power generation facilities, intangible assets, investment properties.
- **NOT** *qualifying assets*: financial assets & inventories that are manufactured/otherwise produced over short period of time OR assets ready for their intended use/sale when acquired.

Directly attributable borrowing costs = borrowing costs that would have been avoided if expenditure on qualifying asset had not been made [may be difficult to identify direct relationship (e.g., centrally co-ordinated financing) → use judgment].

When carrying amount or expected ultimate cost of qualifying asset > recoverable amount or NRV → write down/off carrying amount in accordance with requirements of other Standards (also written back in accordance with those other Standards in certain circumstances).

BORROWING COSTS ELIGIBLE FOR CAPITALIZATION

Funds borrowed specifically to obtain a specific qualifying asset:

- Directly related borrowing costs readily identifiable.
- *Borrowing costs* eligible for capitalization = actual costs incurred on that borrowing during period LESS investment income on temporary investment of those borrowings.

Funds borrowed for general purposes and used for purpose of obtaining qualifying asset:

- *Borrowing costs* eligible for capitalization = *Capitalization rate* X expenditures on that asset.
- Amount capitalized <= borrowing costs incurred during period.

Capitalization rate = weighted average of borrowing costs applicable to outstanding borrowings during period OTHER THAN borrowings made specifically to obtain qualifying asset.

$$\frac{\text{Total general borrowing costs for the period}}{\text{Weighted average total general borrowings outstanding in period}}$$

COMMENCEMENT OF CAPITALIZATION

- Begin capitalizing borrowing costs when entity first meets ALL the following conditions (i.e., the **commencement date**):
  - It incurs expenditures for the asset.
  - It incurs borrowing costs.
  - It undertakes activities necessary to prepare asset for its intended use.
- Expenditures on qualifying asset include ONLY those expenditures that have resulted in payments of cash, transfers of other assets/the assumption of interest-bearing liabilities LESS progress payments and grants received in connection with asset.
- Activities necessary to prepare asset for its intended use/sale encompass more than physical construction.
  - Includes: technical & administrative work prior to commencement of physical construction (e.g., obtaining permits prior to commencement of physical construction).
  - Excludes: holding of an asset when no production/development that changes asset's condition.

SUSPENSION OF CAPITALIZATION

- Suspend capitalizing if active development suspended for extended period (because cost of holding partially completed assets do not qualify for capitalization).
- DO NOT normally suspend during period of substantial technical and administrative work.
- DO NOT suspend when temporary delay is necessary part of process (e.g., high water levels may delay bridge construction).

CESSATION OF CAPITALIZATION

- Cease capitalizing when substantially all activities necessary to prepare qualifying asset for intended use/sale are complete (e.g., minor administrative work or only decoration left).
- When construction of qualifying asset completed in parts & each part is usable while construction continues on other parts→ cease capitalizing when substantially all activities necessary to prepare that part for its intended use/sale is complete.