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ASB

(By e mail)

Dear Sirs,

**Property, plant and equipment; Borrowing costs (FRED 29)**

I am writing on behalf of my firm to set out our responses to FRED 29.

- ASB (i) Do you agree with the proposal to issue new UK standards on property, plant and equipment and borrowing costs when the IASB issues the revised IAS 16, *unless* it becomes clear that further changes to IAS 16 are likely by 2005 as a result of the revaluation project?

We agree that, if it is likely that further changes will be forthcoming from the IASB, the implementation of FRED 29 should be delayed.

This is because the volume of standards issued by the ASB will be fairly high between now and 2005, and it would be simpler to issue one standard in respect of Fixed Assets rather than issuing one and then amending it at a later date.

We consider that the existing standards cover all matters relating to matters covered by FRED 29.

- ASB (ii) The international exposure draft on property, plant and equipment proposes that residual values used in the calculation of depreciable amount should be reviewed at each balance sheet date and revised to reflect current estimates. FRS 15 generally requires prices at the date of acquisition or latest valuation to be used; hence, depreciation expense on a historical cost basis is not reduced by inflation in residual values. Do you agree or disagree with the proposed international approach?

We disagree with the international approach. The reconsideration of residual values would create additional work for those preparing accounts and we consider that the extra information given would not be of great value.

Inflation in most industrialized countries is not at large % levels, and therefore any adjustment arising from a revision in residual value is unlikely to have a material effect on the accounts.

ASB (iii) IAS 16 does not address the use of renewals accounting in respect of certain infrastructure assets. Do you believe that the absence of the guidance in FRS 15 would prevent entities from using renewals accounting as a method of estimating depreciation? Should UK entities be permitted to continue to use renewals accounting?

We believe that the UK should be entitled to contour to use renewals accounting in the few circumstances where it gives a true and fair view.

Although we do not consider the FRED as drafted would prevent renewals accounting, FRS 15 defines when it may be used and strict conditions. These are absent from the FRED and we consider this may result in abuse by those preparing accounts. For this reason, we would like to have the guidance from FRS15 incorporated in any standard such as FRED 29.

ASB (iv) What are your views on the differences between the requirements of FRS 15 and IAS 16 concerning revaluation (as described in paragraphs 10 to 17 of the Preface to the FRED)?

We consider that users of accounts would be able to appreciate revaluations in accounts that are based upon market valuations, rather than the concept of fair valuations. We therefore prefer the IAS principle of revaluation's being based upon market valuations, rather than existing use valuations, as this would simplify the treatment of valuations in the accounts.

We consider that guidance should be incorporated in the FRED to set out the frequency of valuations. As drafted, this is left to the judgment of those preparing accounts, which could be influenced by various factors. By setting out the period over which valuations should be carried out, as in FRS15, those preparing accounts are forced to carry out the valuations or disclose the non-compliance with accounting standards.

We also consider the detailed guidance in FRS15 relating to valuations, and appendix 1 to be useful. A similar appendix and detail should be attached to the FRED.

We believe that the treatment of revaluation losses and surpluses is inconsistent. The current rules should apply, so that a revaluation loss exceeding a previous

surplus is recognized in the statement of recognized gains or losses. This assists in producing statements that show the true effect of revaluations.

For the above reason, we also consider that all impairment losses should be shown in the profit and loss account, and not in the Statement of Gain and Losses.

ASB (v) Are there any other aspects of the differences between the proposed standards and current UK accounting requirements that you wish to comment on?

No.

ASB (vi) Do you agree with the ASB's proposal, as a transitional measure (see paragraph 18 above), that the present exemption in FRS 15 in respect of insurance companies should be retained in a new UK standard based on IAS 16 revised pending the outcome of the IASB's projects on insurance and reporting financial performance?

We agree that the present exemption should be incorporated in the FRED.

ASB (vii) The transitional arrangements for the first-time application of FRS 15 allowed an entity that does not adopt a policy of revaluation to retain carrying amounts reflecting previous revaluations instead of restating the carrying amounts to historical cost (see paragraph 19 above). Do you believe that a transitional arrangement should be included in a new UK standard to allow entities that adopted FRS 15's transitional arrangement to continue to recognize the carrying amounts under that arrangement?

We agree that the transitional arrangements regarding FRS15 should be maintained.

ASB (viii) Do you believe that ASB should consider any other transitional arrangements?

No.

ASB (ix) Are there any other aspects of the draft standard on property, plant and equipment that the ASB should request the IASB to review when finalizing the revised IAS 16?

No.

ASB (x) Do you agree that the capitalization of borrowing costs should remain optional? If you had to choose between mandatory capitalization and prohibition of capitalization, which would you support and why?

We consider that there should be no optional choice between the methods of interest capitalization, so those users of accounts can easily compare one entity with another.

We would support the mandatory capitalization of interest, due to the fact that this would show the “true” cost of bringing an asset into existence.

ASB (xi) Do you agree that paragraph 5(e) of IAS 23, which allows certain exchange differences to be capitalised, should be deleted in the draft standard on borrowing costs?

We believe that all exchange differences should be shown on the profit and loss account. Paragraph 5(e) should therefore be deleted.

ASB (xii) What are your views on the difference between IAS 23 and FRS 15 referred to in paragraph 24 of the Preface to the FRED concerning borrowing costs eligible for capitalisation?

We consider that it is correct to show the true cost of borrowing within fixed assets. Temporary investment income is a matter of policy of a company, and therefore the effect of the company’s money management policy should be shown in the profit and loss account, as currently required in FRS 15.

The treatment of IAS23 in relation to this matter would result in a difference in the capitalised figure, depending on the amount of borrowings received at the start of the project.

ASB (xiii) Do you have any comments on IAS 23 that you wish the ASB to bring to the IASB’s attention?

No.

The IASB has asked commentators to respond to the following questions on the proposed changes to IAS 16:

IASB (i) Do you agree that all exchanges of items of *property, plant and equipment* should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably (see paragraphs 21 and 21A of the [draft] FRS on property, plant and equipment)?

We believe this would enable transactions to be reported correctly, showing a true and fair view and agree to the incorporation of such a requirement.

IASB (ii) Do you agree that all exchanges of *intangible assets* should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably?

We believe this would enable transactions to be reported correctly, showing a true and fair view and agree to the incorporation of such a requirement.

IASB (iii) Do you agree that depreciation of an item of property, plant and equipment should not cease when it becomes temporarily idle or is retired from active use and held

for disposal (see paragraph 59 of the [draft] FRS on property, plant and equipment)?

We believe that when an asset ceases to be used, the asset should be written down immediately to its recoverable value and an impairment review carried out if necessary. Depreciation should therefore cease at that point.

However, if an asset had been temporarily idle, then we suggest that the correct treatment be for depreciation to continue.

Yours truly,

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Technical Partner