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**International
Accounting Standards
Board**

This document is provided as a convenience to observers at IASB meetings, to assist them in following the Board's discussion. It does not represent an official position of the IASB. Board positions are set out in Standards.

These notes are based on the staff papers prepared for the IASB. Paragraph numbers correspond to paragraph numbers used in the IASB papers. However, because these notes are less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

Board Meeting: 18 July 2007, London

Project: Annual Improvements

Subject: IAS 23 – Components of borrowing costs
(Agenda paper 5G)

1. The staff have identified that the following issue would be most appropriately resolved via the annual improvements process.

Issue: Should the components of borrowing costs given in IAS 23 *Borrowing Costs* be revised to make reference to the guidance in IAS 39 *Financial Instruments: Recognition and Measurement* relating to effective interest rate?

Staff recommendation

2. The staff recommends that the Board:
 - should add this issue to the annual improvements project; and
 - should amend IAS 23 as proposed in paragraph 8 of this paper.

Background

3. The staff has been notified of a potential inconsistency in the components of borrowing costs between IAS 23 and IAS 39.

IAS 23 guidance

4. Paragraph 6 of IAS 23 provides a list of the components of borrowing costs. These are:
 - (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 IAS 17 *Leases*; and
 - (e) exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs.
5. The staff notes that items (a) to (c) are broadly equivalent to the components of interest expense calculated using the effective interest method in accordance with IAS 39. The exception is in respect of ‘ancillary costs’ in item (c). The staff also notes however that there is no definition of ‘ancillary costs’ provided in IFRS literature. The staff believes that consistency between standards would be improved if items (a) to (c) above were replaced with a cross reference to interest expense calculated in accordance with the effective interest method as defined in IAS 39.

Staff recommendation

6. The staff recommends that IAS 23 be amended as proposed in paragraph 8 to align the description of borrowing costs with the definition of interest expense as computed using the effective interest method in IAS 39.
7. **Does the Board agree?**

Drafting

8. The staff recommend that IAS 23 should be amended as follows:

Definitions

...

- 6 Borrowing costs may include:
 - (a) interest expense calculated using the effective interest rate method as described in IAS 39 *Financial Instruments: Recognition and Measurement* ~~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;~~
 - (b) finance charges in respect of finance leases recognised in accordance with IAS 17 *Leases*; and
 - (c) exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs.

Basis for Conclusions on Proposed Amendments to IAS 23 Borrowing Costs

This Basis for Conclusions accompanies, but is not part of, the draft amendments.

Definitions

- BC1 The Board identified a potential inconsistency in the components of borrowing costs between IAS 23 and IAS 39.
- BC2 The Board notes that components of borrowing costs set out in items (a) to (c) of paragraph 6 of IAS 23 *Borrowing Costs* are broadly equivalent to the components of interest expense calculated using the effective interest method in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*. The exception is in respect of ‘ancillary costs’ in item (c), for which the Board noted that there is no definition in IFRS literature.
- BC3 The Board decided that consistency between standards would be improved if items (a) to (c) in paragraph 6 of IAS 23 were replaced with a reference to interest expense calculated in accordance with the effective interest method as defined in IAS 39.