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Project	<b>Review of tentative agenda decision from May 2011</b>
Topic	<b>IAS 16 <i>Property, Plant and Equipment</i>—cost of testing</b>

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## **Introduction**

1. The IFRS Interpretations Committee (the Interpretations Committee) received a request to clarify the accounting for sales proceeds received from testing an asset before it is ready for its intended use.

## **Purpose of the paper**

2. The objective of this paper is:
  - (a) to provide background information on the issue;
  - (b) to provide feedback on comments received on the tentative agenda decision from the Interpretations Committee’s meeting in May 2011;
  - (c) to make a recommendation that the Interpretations Committee should proceed with the agenda decision; and
  - (d) to ask if the Interpretations Committee agrees with the staff’s recommendation.

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This paper has been prepared by the technical staff of the IFRS Foundation for discussion at a public meeting of the IFRS Interpretations Committee.

The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the IFRS Interpretations Committee or the IASB. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination.

Decisions made by the IFRS Interpretations Committee are reported in *IFRIC Update*.

Interpretations are published only after the IFRS Interpretations Committee and the Board have each completed their full due process, including appropriate public consultation and formal voting procedures. The approval of an Interpretation by the Board is reported in *IASB Update*.

IASB Staff paper

**Background**

3. The context of the question in the submission is set out in agenda paper 10<sup>1</sup>, which was presented to the Interpretations Committee at its meeting in May 2011.
4. The question that arises from this specific case is if, with respect to paragraph 17(e) of IAS 16, revenue from products produced from completed plants and sold on the market could be used to offset the costs of testing the other plants that are still in the commissioning phase. That is, whether such revenues could be accounted for as a reduction in the cost of plants being constructed, rather than recognised as revenue in profit or loss.
5. The Interpretations Committee noted that paragraph 17(e) of IAS 16 applies to an item of property, plant and equipment, and therefore, in relation to the fact pattern included in the submission, is likely to apply separately to each individual plant. It also observed that the ‘commercial production date’ referred to in the submission for the whole complex was a different concept from the ‘ready for intended use’ assessment in paragraph 16(b) of IAS 16. The Interpretations Committee believes that the guidance in IAS 16 is sufficient to identify the date at which an item of property, plant and equipment is ‘ready for intended use’ and, therefore, to distinguish proceeds that offset the costs of testing the asset from revenue from commercial production.
6. Consequently, the Interpretations Committee tentatively decided in May that it should not take the issue to its agenda.

**Comments received on the tentative agenda decision published in May IFRIC Update**

7. We have received two comment letters<sup>2</sup> with respect to the tentative agenda decision published in the May 2011 IFRIC Update on this issue. While those

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<sup>1</sup> <http://www.ifrs.org/NR/rdonlyres/0EAF3D82-C5D9-4C27-854A-1356114AFC8C/0/101105ob10IAS16Costsoftesting.pdf>

<sup>2</sup> AcSB and DTT

IASB Staff paper

letters fully support the decision not to take the issue to the Committee's agenda, one of the letters<sup>3</sup> provides additional comments that we analyse in the following paragraphs.

8. While the constituent agrees with the decision not to take the issue to the Interpretations Committee's agenda, the constituent expresses the following concerns:
  - (a) it is inappropriate for the Committee to comment on the likely accounting treatment for a submitted fact pattern 'likely to apply separately to each individual plant'; and
  - (b) the term "ready for intended use" should be removed because this term is not used in IAS 16. Using this term would be interpreting the requirement in paragraph 16(b) of IAS 16 based on the use of this term in IAS 23 *Borrowing Costs*.
9. With respect to the concern expressed in subparagraph (a) of paragraph 8 above, we agree that the wording could be improved. We also note that the Interpretations Committee was in agreement with the first sentence in paragraph 10 of agenda paper 10 that was presented at the meeting in May 2011. More specifically, the Committee agreed that paragraph 17(e) of IAS 16 applies separately to each individual plant. Therefore, we propose improved wording in Appendix A to this paper.
10. With respect to the concern expressed in subparagraph (b) of paragraph 8 above, we note that paragraph 55 of IAS 16 uses 'available for use' when meaning 'in the location and condition necessary for it to be capable of operating in the manner intended by management'. We believe that 'ready for intended use' has the same meaning.
11. In addition, we believe that the terminology 'intended use or sale' (eg see paragraph 19 of IAS 23) is used in IAS 23 with the same meaning as in IAS 16 where the asset is 'in the location and condition necessary for it to be capable of

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<sup>3</sup> AcSB

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operating in the manner intended by management'. We are not aware of diverging views on that terminology.

12. Consequently, with respect to the concern expressed in subparagraph (b) of paragraph 8 above, we agree that the wording of the agenda decision should be consistent with the terminology used in IAS 16. Therefore, we propose improved wording in Appendix A to this paper.

**Staff's recommendation**

13. We recommend that the Interpretations Committee should confirm that it does not take the issue to its agenda and should proceed with the agenda decision with amendments proposed in Appendix A to this paper.

**Question to the Interpretations Committee**

Question—staff's recommendation
Does the Interpretations Committee agree with the staff's recommendation?

IASB Staff paper  
Appendix A

## Appendix A – Wording for the agenda decision

**IAS 16 *Property, Plant and Equipment*—cost of testing**

The Interpretations Committee received a request to clarify the accounting for sales proceeds from testing an asset before it is ready for commercial production. The fact pattern in the submission is that of an industrial group with several autonomous plants being ready available for ~~their intended~~ use at different times. This group is subject to regulation that requires the group to identify a 'commercial production date' for the whole industrial complex. The question asked of the Committee is if the proceeds from those plants already in operation can be offset against the costs of testing those plants that are not yet ready available for ~~their intended~~ use.

The Committee noted that paragraph 17(e) of IAS 16 applies separately to ~~an~~ each item of property, plant and equipment, ~~and, therefore, in relation to the fact pattern included in the submission, is likely to apply separately to each individual plant.~~ It also observed that the 'commercial production date' referred to in the submission for the whole complex was a different concept from the 'ready available for ~~intended~~ use' assessment in paragraph 16(b) of IAS 16. The Committee ~~believes~~ thinks that the guidance in IAS 16 is sufficient to identify the date at which an item of property, plant and equipment is 'ready available for ~~intended~~ use' and, therefore, to distinguish proceeds that reduce ~~offset~~ costs of testing an the asset from revenue from commercial production.

As a result, the Committee does not expect diversity to arise in practice and therefore decided not to add this issue to its agenda.

June 16, 2011

(by e-mail to [ifric@ifrs.org](mailto:ifric@ifrs.org))

IFRS Interpretations Committee  
30 Cannon Street,  
London EC4M 6XH  
United Kingdom

Dear Sirs,

**Re: Tentative agenda decision on IAS 16 *Property, Plant and Equipment* – cost of testing**

This letter is the response of the staff of the Canadian Accounting Standards Board (AcSB) to the IFRS Interpretations Committee's tentative agenda decision on the accounting for sales proceeds received from testing an asset under IAS 16 *Property, Plant and Equipment*. This tentative agenda decision was published in the May 2011 IFRIC Update.

The views expressed in this letter take into account comments from individual members of the AcSB staff but do not necessarily represent a common view of the AcSB or its staff. Views of the AcSB are developed only through due process.

We agree with the Committee's decision not to add this item to its agenda for the reasons provided in the tentative agenda decision. However, we think the tentative agenda decision needs to be modified as follows:

- We recommend removing the statement about the likely application of IAS 16 because we think it is inappropriate for the Committee to comment on the likely accounting treatment for a submitted fact pattern.

- We recommend removing the term “ready for intended use” because this term is not used in IAS 16 and would be interpreting the requirement in paragraph 16(b) of IAS 16 based on the use of this term in IAS 23 *Borrowing Costs*.

The Appendix reflects our recommendations and drafting suggestions.

We would be pleased to provide more detail if you require. If so, please contact me or Kathryn Ingram, Principal, Accounting Standards at +1 416 204-3475 (e-mail [kathryn.ingram@cica.ca](mailto:kathryn.ingram@cica.ca)).

Yours truly,



Peter Martin, CA  
Director,  
Accounting Standards

## Appendix

We suggest clarifying the tentative agenda decision as follows:

### **IAS 16 *Property, Plant and Equipment* – cost of testing**

The Interpretations Committee received a request to clarify the accounting for sales proceeds from testing an asset before it is ready for commercial production. The fact pattern in the submission is of an industrial group with several autonomous plants being ready for their intended use at different times. This group is subject to a regulation that requires the group to identify a ‘commercial production date’ for the whole industrial complex. The question asked of the Committee is whether the proceeds from those plants already in operation can be offset against the costs of testing those plants that are not yet ready for their intended use.

The Committee noted that paragraph 17(e) of IAS 16 applies to an item of property, plant and equipment ~~and in relation to the fact pattern included in the submission, is likely to apply separately to each individual plant.~~ They Committee also observed that the ‘commercial production date’ referred to in the submission for the whole complex was a different concept from the ~~‘ready for intended use’~~ assessment in paragraph 16(b) of IAS 16 (i.e. “bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management”). The Committee ~~believes~~ thinks that the guidance in IAS 16 is sufficient to ~~identify the date at which an item of property, plant and equipment is ‘ready for intended use’ and therefore~~ to distinguish proceeds that ~~reduce~~ offset costs of testing ~~an~~ the asset from revenue from commercial production.

As a result, the Committee does not expect diversity to arise in practice and therefore [decided] not to add this issue to its agenda.



Mr Robert Garnett  
Chairman  
International Financial Reporting Interpretations Committee  
30 Cannon Street  
London  
United Kingdom  
EC4M 6XH

Email: ifric@ifrs.org

20 June 2011

Dear Mr Garnett,

**Tentative agenda decision: IAS 16: Property, Plant and Equipment – Cost of testing**  
**Tentative agenda decision: IAS 19: Employee Benefits – Defined contribution plans with vesting conditions**

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretation Committee's publication in the May 2011 *IFRIC Update* of the tentative decision not to take onto the IFRIC's agenda requests for Interpretations of IAS 16, *Property, Plant and Equipment*, with respect to sales proceeds from testing an asset before it is ready for commercial production and of IAS 19, *Employee Benefits*, with respect to the impact of vesting conditions on the accounting for defined contribution plans.

We agree with the IFRS Interpretations Committee's decision not to add these items onto its agenda for the reasons set out in the tentative agenda decisions.

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0)20 7007 0884.

Yours sincerely,



**Veronica Poole**  
Global Managing Director  
IFRS Technical