STAFF PAPER

29-30 January 2014

IFRS Interpretations Committee Meeting

Project	**IAS 16 *Property, Plant and Equipment***
Paper topic	Disclosure of carrying amount information for assets stated at revalued amounts

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Introduction

1. The IFRS Interpretations Committee (the Interpretations Committee) received a request inquiring whether an entity is required reflect the capitalisation of borrowing costs to meet the disclosure requirement in IAS 16 *Property, Plant and Equipment* paragraph 77(e) for assets stated at revalued amounts for which borrowing costs are not capitalised in accordance with IAS 23 *Borrowing Costs* paragraph 4(a). The submitter asserted that the capitalisation of borrowing costs for these assets to meet disclosure requirements is burdensome, and suggested that it should not be a requirement of IAS 16 to capitalise these costs.

2. The structure of this paper is as follows:

   (a) Issue

   (b) Staff analysis

   (c) Recommendation

   (d) Appendix A: Original submission

Issue

3. IAS 16 paragraph 77(e) requires disclosure of the carrying amount that would have been recognised under the cost model for assets accounted for under the revaluation model:

> 77 If items of property, plant and equipment are stated at revalued amounts, the following shall be disclosed in addition to the disclosures required by IFRS 13:
>
> …
>
> (e) for each revalued class of property, plant and equipment, the carrying amount that would have been recognised had the assets been carried under the cost model; and
>
> …

4. The submitter noted that in IAS 23 paragraph 4(a) an entity is not required to capitalise borrowing costs for qualifying assets measured at fair value:

> 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
>
> …

5. The reason behind this exclusion in IAS 23 results from the IASB's reasoning that the measurement of assets at fair value will not be affected by borrowing costs incurred during construction or production. This is reflected in the Basis for Conclusions to IAS 23:

> 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.

6. The submitter was of the view that the explanation in the Basis for Conclusions that borrowing cost requirements are "unnecessary" for assets at fair value implied that it is not necessary to capitalise borrowing costs for the disclosure requirement in IAS 16.

7. Accordingly, the submitter asked how the requirement of IAS 16 paragraph 77(e) should be applied to qualifying assets measured at fair value accounted for under the revaluation model. The submitter stated that a "literal reading" of the Standards would support the view that the disclosure given should reflect the capitalisation of borrowing costs. However, the submitter asserted that capitalisation of borrowing costs for such assets was costly and of questionable relevance. It therefore supported the view that the disclosure should not be required and that the requirement in paragraph 77(e) should be deleted.

8. A copy of the submission is included in Appendix A of this Agenda Paper.

Staff analysis

9. We think that IAS 16 is clear in its requirement in paragraph 77(e) that the carrying amount that would have been recognised under the cost model shall be disclosed for assets carried under the revaluation model. As a result, we think that the disclosure has to reflect the amount that the assets would have been stated at had the cost model been applied and borrowing costs been capitalised. The

submitter itself noted that a reading of the Standard results in this conclusion, and so we do not think the interpretation of this requirement is of issue. Rather, the concern raised by the submitter is whether the disclosure requirement in paragraph 77(e) should be deleted to ease perceived operational concerns.

10. Paragraph BC4 of the Basis for Conclusions to IAS 23 says that the measurement of assets at fair value will not be affected by the amount of borrowing costs incurred. The submitter references this as reasoning for why borrowing costs should not be required to be capitalised in the disclosure requirement. We do not agree with this conclusion. That borrowing costs incurred do not affect fair value measurement is a separate issue to the disclosure of information about measurement at cost. The capitalisation of borrowing costs on an asset at fair value is unnecessary because fair value is a market-based measurement under which an entity takes into account the characteristics of an asset that market participants would when pricing it. Additional factors, such as borrowing costs, do not need to be added in order to come to a fair value. IAS 23, however, mandates the capitalisation of borrowing costs for qualifying assets measured at cost.

11. We note that the disclosure in IAS 16 is consistent with IAS 38 *Intangible Assets*, which also features an accounting policy choice between a cost model and a revaluation model. Like IAS 16, IAS 38 paragraph 142(a)(iii) requires disclosure of the carrying amount that would have been recognised under the cost model for intangible assets carried under the revaluation model.

12. We note that including capitalised borrowing costs in a disclosure of the amount that would have been recognised under the cost model is relevant for retaining comparability among entities. The revaluation model is an option, and the disclosure in paragraph 77(e) is needed if there is to be comparability with assets carried under the cost model. Providing this disclosure enables users of financial statements to compare the assets of an entity that applies the revaluation model with those of other entities that use the cost model. Hence, we do not think that removing this disclosure requirement would improve financial reporting.

Feedback from users of financial statements

13. This issue was presented to a users' representative organisation in the submitter's jurisdiction, from which four responses were received. Those respondents felt that the disclosure requirement should be retained as it currently stands (ie that the entity shall disclose the carrying amount had the cost model been applied). This was because comparability was considered important, and that such comparability would be lost if the disclosure requirement was deleted or modified to exclude borrowing costs for entities that carry assets under the revaluation model. As mentioned above, we also think that the disclosure is useful for comparability reasons, and that financial reporting would not be improved by its removal.

IFRS Interpretations Committee agenda criteria

14. The following lists the agenda criteria used to assess whether an issue should be addressed by the Interpretations Committee.

Agenda criteria

We should address issues (5.16):	
that have widespread effect and have, or are expected to have, a material effect on those affected.	Yes. The disclosure requirement of IAS 16 paragraph 77(e) applies to any entity that applies the revaluation model for PPE and intangible assets.
where financial reporting would be improved through the elimination, or reduction, of diverse reporting methods.	No. We do not think financial reporting would be improved by an elimination of the disclosure requirement of IAS 16 paragraph 77(e), and we do not think it would affect the diversity of reporting as the requirement is clear. Such elimination would rather serve to reduce perceived operational concerns.
that can be resolved efficiently within the confines of existing IFRSs and the *Conceptual Framework for Financial Reporting*.	Yes. We think that a change to a disclosure requirement of IAS 16 paragraph 77(e) could be readily resolved within the confines of existing IFRS.
In addition:	
Can the Interpretations Committee address this issue in an efficient manner (5.17)	Yes. This issue could be resolved in an efficient matter.

Will it be effective for a reasonable time period (5.21)? Only take on the topic of a forthcoming Standard if short-term improvements are justified.	Yes. As an amendment of IAS 16 we expect that it would be effective for a reasonable time.
Additional criteria for annual improvements	
In addition to the implementation and maintenance criteria, an annual improvement should (6.11, 6.12):	
• Replace unclear wording; • Provide missing guidance; or • Correct minor unintended consequences, oversights or conflict.	We do not think that the requirement in IAS 16 paragraph 77(e) is unclear, nor do we think there is missing guidance. Furthermore, we do not think that this disclosure requirement was unintended consequence in conflict with IAS 23.
Not change an existing principle or propose a new principle	
Not be so fundamental that the IASB will have to meet several times to conclude (6.14)	We do not consider this a fundamental issue.

15. The staff think that this issue does not meet the agenda criteria (including the additional criteria for annual improvements) of the Interpretations Committee.

Recommendation

16. In the light of the existing requirements in IFRS, and our assessment of the Interpretations Committee's agenda criteria, neither an Interpretation nor an amendment to IFRSs is necessary. We therefore recommend that the Interpretations Committee should not take this issue onto its agenda.

Question to the Interpretations Committee
Do you agree with the staff recommendation not to add this topic to the Interpretation Committee's agenda? Do you agree with the wording of the tentative agenda decision?

Tentative agenda decision

17. We propose the following wording for the agenda decision:

IAS 16 *Property, Plant and Equipment*—Disclosure of carrying amounts under the cost model

The Interpretations Committee received a request for clarification about IAS 16 *Property, Plant and Equipment*. The submission relates to whether an entity is required to reflect the capitalisation of borrowing costs to meet the disclosure requirement in IAS 16 *Property, Plant and Equipment* paragraph 77(e) for assets stated at revalued amounts for which borrowing costs are not capitalised in accordance with IAS 23 *Borrowing Costs* paragraph 4(a).

The submitter asserted that the capitalisation of borrowing costs for these assets to meet disclosure requirements is burdensome, and suggested that it should not be a requirement of IAS 16 to capitalise these costs.

The Interpretations Committee noted that the requirements in IAS 16 paragraph 77(e) are clear. This paragraph requires an entity to disclose the amount at which assets stated at revalued amounts would have been stated at had those assets been carried under the cost model. The amount to be disclosed includes borrowing costs capitalised in accordance with IAS 23. The Interpretations Committee also noted that this requirement enables users of financial statements to compare between entities that apply the cost model in IAS 16 and those that apply the revaluation model.

The Interpretations Committee determined that, in the light of the existing IFRS requirements, neither an Interpretation nor an amendment to IFRSs was necessary and consequently [decided] not to add this issue to its agenda.

Appendix A—original submission

IFRIC Agenda Request – IAS 16 cost disclosure under the revaluation model

Background

IAS 16 - *Property, Plant and Equipment* (PPE) permits application of the revaluation model. Paragraph 31 states that the revalued amount is the fair value at date of revaluation less any subsequent depreciation and impairment losses. Revaluations are meant to be carried out with sufficient regularity to ensure that the carrying amount does not differ materially from fair value at the end of the reporting period. If the revaluation model is applied, paragraph 77(e) requires disclosure of the carrying amount that would have been recognized had the cost model been applied. IAS 16 is silent on the capitalisation of borrowing costs, since this is addressed in IAS 23 - *Borrowing Costs*.

According to IAS 23 paragraph 4(a), an entity is not required to apply IAS 23 in respect of qualifying assets measured at fair value, for example biological assets. BC 4 explains the reason for this. It states that the measurement of such assets will not be affected by the amount of borrowing costs incurred during their construction or production. Therefore, requirements on how to account for borrowing costs are unnecessary.

Accordingly, we believe that for items of PPE which are qualifying assets and which are carried at revalued amount, it is not necessary to capitalise borrowing costs.

Issue

If borrowing costs are not capitalised, how should the requirements of IAS 16.77(e) be applied? Does the reference to the 'cost model' in IAS 16 require capitalisation of borrowing costs for the note disclosure?

View 1

No. It is very burdensome for preparers to be required to capitalise borrowing costs just for note disclosures. It would counter the relief provided in IAS 23.4(a) for recognition and measurement purposes.

View 2

Yes. Had the cost model been applied borrowing costs would have been required to be capitalised.

Reason for IFRIC to address the issue

Much debate has been had in our jurisdiction as well as with parties internationally about the intention of IAS 16.77(e) and what the correct application should be. A literal reading of IAS 16 would lead to view 2, which in our view results in unnecessary and costly disclosure. We therefore support View 1 and propose that IAS 16 be amended accordingly. In addition, notwithstanding the outcome of this proposal, we question the relevance of the disclosure required by IAS 16.77(e) and propose that it be deleted.