

Exposure Draft

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February 2009

Proposed Amendments to Australian Accounting Standards – Borrowing Costs of Not-for-Profit Public Sector Entities

[AASB 1, AASB 111 & AASB 123]

Prepared by the
Australian Accounting Standards Board



Australian Government

**Australian Accounting
Standards Board**

Commenting on this Exposure Draft

Comments on this Exposure Draft are requested by 3 April 2009. Comments should be addressed to:

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All non-confidential submissions to the AASB will be made available to the public on the AASB website: www.aasb.gov.au.

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AASB 2009-X AMENDMENTS TO AUSTRALIAN ACCOUNTING
STANDARDS – BORROWING COSTS OF NOT-FOR-PROFIT PUBLIC
SECTOR ENTITIES**

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[Draft] Australian Accounting Standard AASB 2009-X *Amendments to Australian Accounting Standards – Borrowing Costs of Not-for-Profit Public Sector Entities* is set out in paragraphs 1 – 9. All the paragraphs have equal authority. Paragraphs in **bold type** state the main principles. AASB 2009-X is to be read in the context of other Australian Accounting Standards, including AASB 1048 *Interpretation and Application of Standards*, which identifies the Australian Accounting Interpretations. In the absence of explicit guidance, AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies.

PREFACE

Background

Australian Accounting Standards

The Australian Accounting Standards Board (AASB) makes Australian Accounting Standards, including Interpretations, to be applied by:

- (a) entities required by the *Corporations Act 2001* to prepare financial reports;
- (b) governments in preparing financial statements for the whole of government and the General Government Sector (GGS); and
- (c) entities in the private or public for-profit or not-for-profit sectors that are reporting entities or that prepare general purpose financial statements.

Australian Accounting Standards incorporate International Financial Reporting Standards (IFRSs), including Interpretations, issued by the International Accounting Standards Board (IASB), with the addition of paragraphs on the applicability of each Standard in the Australian environment.

Australian Accounting Standards also include requirements that are specific to Australian entities. These requirements may be located in Australian Accounting Standards that incorporate IFRSs or in other Australian Accounting Standards. In most instances, these requirements are either restricted to the not-for-profit or public sectors or include additional disclosures that address domestic, regulatory or other issues. In developing requirements for public sector entities, the AASB considers the requirements of International Public Sector Accounting Standards (IPSASs), as issued by the International Public Sector Accounting Standards Board (IPSASB) of the International Federation of Accountants.

Private sector for-profit entities complying with Australian Accounting Standards will simultaneously comply with IFRSs. Many other entities complying with Australian Accounting Standards will also simultaneously comply with IFRSs.

Exposure Drafts

The publication of an Exposure Draft is part of the due process that the AASB follows before making a new or amending an existing Australian Accounting Standard. Exposure Drafts are designed to seek public comment

on the AASB's proposals for new Australian Accounting Standards or amendments to existing Australian Accounting Standards.

Reasons for Issuing this Exposure Draft

This Exposure Draft proposes to amend AASB 123 *Borrowing Costs* (2007, as amended), and consequently AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards* and AASB 111 *Construction Contracts*.

These amendments arise from the AASB's short-term review of the requirement in AASB 123 to capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. Following that review, the AASB decided to reintroduce the option for not-for-profit public sector entities to expense those borrowing costs pending the outcome of:

- (a) the New Zealand Financial Reporting Standards Board's work on the relationship between depreciated replacement cost and borrowing costs. The AASB agreed to participate in that work;
- (b) the AASB's work on developing its *Process for Modifying IFRSs for Application by Not-for-Profit Entities*; and
- (c) the IPSASB's borrowing costs project.

Main Features of this Exposure Draft

Option to Expense Borrowing Costs

In respect of not-for-profit public sector entities, this Exposure Draft proposes to amend AASB 123 by reintroducing the option to expense borrowing costs and thereby allow, subject to the requirements in AASB 1049 *Whole of Government and General Government Sector Financial Reporting*, an entity to choose whether it expenses or capitalises borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset. Consequential disclosures about the accounting policy adopted are also specified.

As a consequence of reintroducing the option, this Standard would also amend AASB 111 to specify that costs that may be attributable to contract activity in general and can be allocated to specific contracts include borrowing costs only when the contractor capitalises borrowing costs in accordance with AASB 123.

Application Date

It is proposed that this Standard be applicable to annual reporting periods beginning on or after 1 January 2009 that end on or after 30 April 2009 with early adoption permitted for annual reporting periods beginning on or after 1 January 2009 that end before 30 April 2009 provided AASB 123 is also adopted for the same period. This proposed Standard is required to be applied when AASB 123 is applied.

Request for Comments

Comments are invited on any of the proposals in this Exposure Draft by 3 April 2009. The AASB would prefer that respondents express a clear overall opinion on whether the proposals, as a whole, are supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on the major issues. The AASB regards supportive and critical comments as essential to a balanced review of the issues and will consider all submissions, whether they address all specific matters, additional issues or only one issue.

Specific Matters for Comment

The AASB would particularly value comments on whether:

- (a) reintroducing the option for not-for-profit public sector entities to expense borrowing costs is appropriate;
- (b) the option should also be reintroduced for not-for-profit private sector entities;
- (c) overall, the proposals would result in financial statements that would be useful to users; and
- (d) the proposals are in the best interest of the Australian economy.

ACCOUNTING STANDARD AASB 2009-X
AMENDMENTS TO AUSTRALIAN ACCOUNTING
STANDARDS – BORROWING COSTS OF
NOT-FOR-PROFIT PUBLIC SECTOR ENTITIES

Objective

- 1 The objective of this Standard is to amend AASB 123 *Borrowing Costs* (2007, as amended), and consequently amend AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards* and AASB 111 *Construction Contracts*, to reintroduce the option for not-for-profit public sector entities to expense borrowing costs.

Application

- 2 **This Standard applies to:**
 - (a) **each entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act and that is a reporting entity;**
 - (b) **general purpose financial statements of each other reporting entity; and**
 - (c) **financial statements that are, or are held out to be, general purpose financial statements.**
- 3 **This Standard applies to annual reporting periods beginning on or after 1 January 2009 that end on or after 30 April 2009.**
- 4 **This Standard may be applied to annual reporting periods beginning on or after 1 January 2009 that end before 30 April 2009 provided AASB 123 is also adopted for the same period. When an entity applies this Standard to such an annual reporting period, it shall disclose that fact. This Standard shall be applied when AASB 123 is applied.**

Amendment to AASB 1

- 5 An Aus footnote is added at the end of the first sentence of paragraph IG23 of AASB 1 as follows:

Notwithstanding paragraph IG23 of this Standard, in accordance with AASB 123 (as amended by AASB 2009-X *Amendments to Australian Accounting Standards – Borrowing Costs of Not-for-Profit Public Sector Entities*) a not-for-profit public sector entity may choose to expense borrowing costs.

Amendment to AASB 111

- 6 Paragraph Aus18.1 is added after paragraph 18 of AASB 111 as follows:

Aus18.1 In respect of not-for-profit public sector entities, costs that may be attributable to contract activity in general and can be allocated to specific contracts also include borrowing costs only when the contractor capitalises borrowing costs in accordance with AASB 123 *Borrowing Costs*.

Amendments to AASB 123

- 7 Paragraph Aus1.0 is added after paragraph 1 of AASB 123 as follows:

Aus1.0 In respect of not-for-profit public sector entities¹, borrowing costs may be expensed in accordance with paragraph Aus8.1.

- 8 Paragraphs Aus8.1 and Aus8.2 are added after paragraph 8 of AASB 123 as follows:

Aus8.1 A not-for-profit public sector entity may elect to recognise borrowing costs as an expense in the period in which they are incurred regardless of how the borrowings are applied.

Aus8.2 In respect of not-for-profit public sector entities, paragraphs 9-26, 27 and 28 apply only when an entity elects to capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset.

¹ In February 2009, the AASB agreed to reintroduce the expense option for not-for-profit public sector entities. The AASB currently has a project on the application of AASB 123 to not-for-profit public sector entities.

9 Paragraph Aus26.1 is added after paragraph 26 of AASB 123 as follows:

Aus26.1 A not-for-profit public sector entity shall disclose the accounting policy adopted for borrowing costs.

BASIS FOR CONCLUSIONS

The Basis for Conclusions accompanies, but is not part of, AASB 2009-X.

Introduction

- BC1 This Basis for Conclusions summarises the Australian Accounting Standard Board's (AASB's) decisions in reaching the conclusions in this Standard. Individual Board members gave greater weight to some factors than to others.

Background

- BC2 The AASB issued AASB 123 *Borrowing Costs* in July 2004 and, consistent with IAS 23 *Borrowing Costs* at that time, thereby allowed entities to choose whether to expense or capitalise borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset.
- BC3 In 2007, the International Accounting Standards Board (IASB) amended IAS 23 to remove the option and prescribe the capitalisation approach. Accordingly, the AASB revised AASB 123 in June 2007 to align with the revised IAS 23.
- BC4 The International Public Sector Accounting Standards Board (IPSASB) issued IPSAS 5 *Borrowing Costs* in May 2000 and also gave the option to expense or capitalise borrowing costs. After the issue of revised IAS 23 in 2007, the IPSASB initiated a project to consider borrowing costs of not-for-profit public sector entities. As part of the project, the IPSASB issued Exposure Draft ED 35 *IPSAS 5 Borrowing Costs (Revised 200X)*. Among its proposals, the IPSASB proposed to not require the capitalisation of borrowing costs.
- BC5 The IPSASB's proposal to retain the expensing option received support from some Australian public sector constituents.

Significant Issues

- BC6 In considering whether to defer the withdrawal of the option of expensing borrowing costs by reintroducing that option, the AASB noted that:
- (a) the New Zealand Financial Reporting Standards Board (FRSB) deferred the application of revised NZ IAS 23

Borrowing Costs (2007) by public benefit entities, thereby retaining the expense option;

- (b) there are issues surrounding the relationship between the revaluation model commonly adopted by not-for-profit public sector entities, the use of depreciated replacement cost within that model and the capitalisation of borrowing costs. The FRSB is undertaking work on the relationship between depreciated replacement cost and borrowing costs. The AASB agreed to participate in that work. The outcome of that work may inform the AASB on how borrowing costs should be treated in the longer term;
- (c) it is still developing its *Process for Modifying IFRSs for Application by Not-for-Profit Entities*, and borrowing costs will provide a test case for that *Process* once it is developed; and
- (d) as noted in paragraph BC4, the IPSASB is undertaking a project on borrowing costs of not-for-profit public sector entities and the IPSASB's Exposure Draft proposes to retain the option to expense borrowing costs.

BC7 Accordingly, the AASB decided to reintroduce the option to expense borrowing costs for not-for-profit public sector entities pending the outcome of the FRSB/AASB work on depreciated replacement cost, the *Process for Modifying IFRSs for Application by Not-for-Profit Entities* and the IPSASB's project on borrowing costs.

Application Date

BC8 This Standard is applicable to annual reporting periods beginning on or after 1 January 2009 that end on or after 30 April 2009 with early adoption permitted for annual reporting periods beginning on or after 1 January 2009 that end before 30 April 2009 provided AASB 123 is also adopted for the same period. This Standard is required to be applied when AASB 123 is applied.

BC9 Paragraphs 3 and 4 relating to application dates enable not-for-profit public sector entities that chose the option to expense borrowing costs under AASB 123 (2004) to continue to apply that option without interruption.