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Dear Mr Boymal

PROPOSED AMENDMENTS TO AASB 123 BORROWING COSTS

The Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) welcomes the opportunity to comment on the above Exposure Draft.

As the Australian Accounting Standards Board (AASB) is aware, HoTARAC is strongly committed to the convergence of Generally Accepted Accounting Principles (GAAP) with Government Finance Statistics (GFS). Under GFS reporting, borrowing costs on qualifying assets are treated as current period interest expenses. Removing the option for public sector entities to expense such borrowing costs will create a further inconsistency between GAAP and GFS.

HoTARAC recognises that it is preferable for the standards to contain the minimum possible number of options. To further this aim, the AASB should establish a formal process for dealing with emerging GAAP-GFS divergences. It is probable that such divergences will increase because of the impending harmonisation of the International Accounting Standards Board's (IASB) conceptual framework with that of the Financial Accounting Standards Board (FASB) of the United States of America (US). Part of that process may require the AASB to approach the Australian Bureau of Statistics to change its GFS accounting treatment where GAAP represents the best conceptual treatment.

There are several other issues for the public sector associated with the proposed removal of the option to directly expense borrowing costs on qualifying assets:

- The majority of Government assets are held at fair value to comply with GFS requirements. Assets at fair value are specifically excluded from the scope of the proposed Standard under paragraph 3A. It is not clear what the impact will be on a qualifying asset passing from the initial measurement provisions of AASB 116 *Cost While Under Construction* to the subsequent measurement provisions (fair value), due to the withdrawal of the expense option. It is not clear whether the AASB intends that depreciated replacement cost, including capitalised borrowing costs, would be fair value.

- The Exposure Draft recognises that it may be difficult to identify a direct relationship between particular borrowings and a qualifying asset. In many jurisdictions, the "Crown", "residual entity" or a particular department, borrows to fund the General Government Sector. Funds are appropriated to individual departments and/or on-passed to General Government Sector entities to fund asset acquisitions. Where funds are received by separate financial reporting entities as revenue or contributions by owners (equity), it would not appear allowable under ED 123 for these reporting entities to capitalise any "capital charge" levied by the Crown for these indirectly borrowed funds. Withdrawal of the expense option may result in these entities disclosing assets at a different cost to the same qualifying asset in the whole-of-government financial report.

- Comparability across time and across entities is one of the key qualitative characteristics of financial reports. Requiring entities to capitalise interest costs for qualifying assets does not promote this characteristic, when there is no similar requirement for non-qualifying assets or for entities that internally fund the acquisition of qualifying assets.

In respect to the specific questions raised by the International Accounting Standards Board regarding the proposed amendment on borrowing costs, HoTARAC offers the following responses:

Question 1

This Exposure Draft proposes to eliminate the option in IAS 23 of recognising immediately as an expense borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset. Do you agree with the proposal? If not, why? What alternative would you propose and why?

HoTARAC does not agree with the proposal for the reasons outlined above and makes the following recommendations:

1. The option to expense should be retained; or failing this

2. An "Aus" paragraph should be inserted into the Standard to retain the option for public sector entities.

Question 2

This Exposure Draft proposes that entities should apply the amendments to borrowing costs for which the commencement date for capitalisation is on or after the effective date. However, an entity would be permitted to designate any date before the effective date and to apply the proposed amendments to borrowing costs relating to all qualifying assets for which the commencement date for capitalisation is on or after that date. Do you agree with the proposal? If not, why? What alternative would you propose and why?

In the event the public sector is not able to retain the expensing option, a single commencement date should apply.

Yours sincerely

Rob Nicholl
ACTING SECRETARY

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