



## Accounting Standards Board

Aldwych House, 71-91 Aldwych, London WC2B 4HN

Telephone: 020 7492 2300 Fax: 020 7492 2301

[www.frc.org.uk/asb](http://www.frc.org.uk/asb)



25 SEP. 2006

Stig Enevoldsen  
Supervisory Board Chairman  
European Financial Reporting Advisory Group  
Avenue des Arts 13-14  
1210 Brussels  
Belgium

19 September 2006

Dear Stig

### **EFRAG's Draft Comment Letter on the IASB Exposure Draft of Proposed Amendment to IAS 23 *Borrowing Costs***

This letter sets out the ASB's comments on EFRAG's draft comment letter on the above IASB Exposure Draft ("ED"). The ASB is submitting its response to the IASB in parallel with this letter and I attach a copy.

The ASB has similar reservations about the implementation of the proposals made in the ED as noted in your draft letter to the IASB. However, we believe the benefit of reducing divergence between IFRS and US GAAP and the elimination of the reconciliation requirement outweigh these concerns. We therefore do not oppose the proposals set out in the exposure draft. As such we recommend that you make the suggested amendments to the fifth paragraph in your draft letter and in the answer to question 1 in the note to the letter.

If you would like any further information on the comments made above or in the Appendix, then please contact Seema Jamil-O'Neill on 020 7492 2422 or myself on 020 7492 2434.

Yours sincerely

Ian Mackintosh  
Chairman  
Accounting Standards Board  
DDI: 020 7 492 2434  
Email: [i.mackintosh@frc-asb.org.uk](mailto:i.mackintosh@frc-asb.org.uk)



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Ms Anne McGeachin  
International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH

19 September 2006

Dear Anne

### **Exposure Draft of Proposed Amendments to IAS 23 *Borrowing Costs***

The UK Accounting Standards Board (ASB) welcomes the opportunity to comment on the International Accounting Standards Board's Exposure Draft (ED) on the Amendment to IAS 23 *Borrowing Costs*.

We do not oppose the proposals in the ED. On balance we support the need for eliminating the reconciliation between IFRS and US GAAP, as currently required by the SEC, and understand that the level of convergence proposed in the ED is sufficient for SEC purposes.

However, we note that:

- although the proposals bring IAS 23 in line with SFAS 34 *Capitalization of Interest Cost* by requiring the companies reporting under IFRS to capitalise borrowing costs there are significant differences in the actual amounts capitalised between the two standards which will not be addressed by these proposals;
- companies currently reporting under both IFRS and US GAAP have the option to capitalise borrowing costs under existing IFRS and as a result the amendment as proposed is unlikely to provide any extra benefit to these companies; and
- the proposals were not arrived at after a comprehensive review of the conceptual basis for capitalising borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset.

Given the above, we recommend that the IASB clarify in the final Basis for Conclusions that the main driver for this amendment is the fact that when it is implemented the SEC would consider IAS 23 and SFAS 34 as 'converged', even though there would remain some significant differences.

We also recommend that the IASB incorporate a more comprehensive review of the strengths and weaknesses of the IFRS and US GAAP requirements in this area in its work programme. We hope that such a review would address some of the points we have raised above.

Please see appendix A for our detailed comments on the specific questions asked in the Exposure Draft.

If you would like any further information on the comments made above or in the Appendix then please contact me or Seema Jamil-O'Neill on 020 7492 2422.

Yours sincerely



Ian Mackintosh  
Chairman  
Accounting Standards Board  
DDI: 020 7492 2434  
Email: [i.mackintosh@frc-asb.org.uk](mailto:i.mackintosh@frc-asb.org.uk)



## APPENDIX

### RESPONSE TO SPECIFIC QUESTIONS IN ED AMENDMENTS TO IAS 23 BORROWING COSTS

**QUESTION 1 - The 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?**

As noted in our letter we do not oppose the proposals. We note that it would remove some inconsistencies between IFRS and US GAAP, namely that companies reporting under IFRS will no longer have a choice of capitalising or expensing borrowing costs. Instead such companies will be required to capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset thus bringing them in line with companies reporting under US GAAP.

We are, however, concerned that the proposals do not eliminate other more significant inconsistencies between the two approaches. In our view these inconsistencies include:

- the definition and measurement of borrowing costs;
- the definition of qualifying assets;
- the capitalisation rate used; and
- the treatment of capitalisation during any interruptions to the production process.

We also note that paragraph BC10 of the Basis for Conclusions asserts that if the asset had been purchased from a third party then the selling price will include the finance cost incurred during the development phase and so the proposals enhance comparability between assets that are internally developed and those acquired from third parties. We disagree with these comments. We believe that full comparability will not be achieved unless the full economic cost of funding is included in the cost of internally developed assets as it is in external prices, regardless of whether ten or a hundred percent has been financed by borrowings. Even then the credit rating of the third party (impacting the interest rates it is charged on its borrowings) and the addition of a profit margin render the internal and external costs incomparable.

However, as noted above, we support the proposed amendment on the pragmatic grounds that it would help eliminate the SEC requirement for the reconciliation between IFRS and US GAAP in this area.

As noted in the covering letter, we recommend that the IASB perform a more comprehensive review of the requirements under IFRS and US GAAP in this area. We hope that such a review will help establish a firm conceptual basis for the treatment of borrowing costs as well as addressing a number of the issues we raise above.

**QUESTION 2 - The Exposure Draft proposes that entities shall apply the amendments to borrowing costs for which the commencement date is on or after the effective date. However, an entity is permitted to designate any date before the effective date and to apply the [draft] 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 proposals? If not, why? What alternative would you propose and why?**

We agree with the Board's assessment that the cost of retrospective application would outweigh the benefits. We also agree with the rationale for allowing entities to apply the amendment from any date before the effective date. Therefore, we would support the transitional provisions.