AS 16 : BORROWING COST

Overview:

[a] Objective of Borrowing Cost

[b] Scope of AS 16

[c] Meaning & Inclusions of Borrowing Cost

[d] Exchange difference on Foreign Currency Borrowings

[e] Recognition &Qualifying Assets

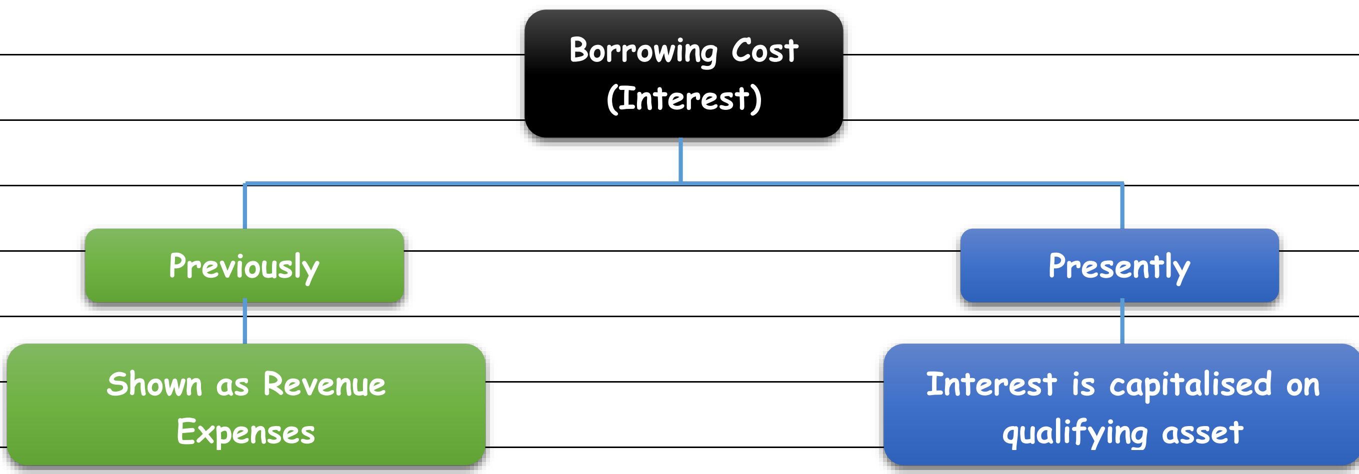
[f] Types of Borrowings.

[g] Capitalisation, Suspension & Cessation of Borrowing Cost

[h] Disclosures

CONCEPT 1 : WHY AS 16? (OBJECTIVE)

- To prescribe accounting for borrowing costs.



CONCEPT 2 : SCOPE

This standard deals only with accounting of borrowing costs;

It does not deal with

- Actual cost incurred
- Imputed Cost (Opportunity/ Notional)

On owner's equity including PSC not classified as liability

Example : Dividend paid on equity shares, cost of issuance of equity, cost on Irredeemable PSC will not be included as borrowing cost.

CONCEPT 3 : MEANING OF BORROWING COST

Borrowing costs are interest & other costs that an entity incurs in connection with the borrowing of funds.

CONCEPT 4 : INCLUSION IN BORROWING COST

- Interest & Commitment charges on Borrowings
- Annual amortisation of premium or discount on Borrowings
- Amortisation of cost incurred for arranging Borrowings
- Finance Charges to acquired assets under Finance Lease
- Exchange difference on foreign borrowings (Para 4e)

CONCEPT 5 : EXCHANGE DIFFERENCE ON FOREIGN CURRENCY BORROWINGS

Para 4e :

Exchange difference

on amount of principal of

foreign currency borrowings

to extent of difference between :

i] Interest on local currency Borrowings

ii] Interest on foreign currency Borrowings

Note :

In other words AS 16

- Deals with
  - Loss on exchange difference compensated by gains due to reduced amount of interest
- Does not deal
  - Gains in exchange difference (taken care of by AS 11)

CONCEPT 6 : RECOGNITION OF BORROWING COST?

Borrowing cost directly attributable to

- Acquisition
- Construction
- Production

- Of qualifying asset
  - Capitalise along with asset
- Of other than qualifying asset
  - Revenue expenditure

CONCEPT 7 : WHAT IS QUALIFYING ASSET?

- ✦ Which takes substantial period of time to get ready for its intended use or sale.
- ✦ Substantial time depends upon facts & circumstances of each case.
- ✦ Ordinarily, substantial period of time = 12 months unless shorter or longer period can be justified on case to case basis.
- ✦ Time which an asset takes technologically & commercially to get ready shall be considered.

Examples of Qualifying Assets :

Sr. no.	Examples of Qualifying Assets	Examples of Non-Qualifying Assets
1]	Manufacturing plants	Investments & inventories produced in large quantities on repetitive basis over short period of time.
2]	Power generation facilities	
3]	Investment properties	Assets ready for intended use or sale on acquisition.

CONCEPT 8 : TYPES OF BORROWINGS

Specific Borrowings

- Borrowing cost should be fully debited to Qualifying Asset.
- Borrowing Cost eligible for capitalization = Actual borrowing cost incurred (-) Income on temporary investment.
- After completion of all qualifying assets, borrowing costs will be charged to P&L.

General Borrowings

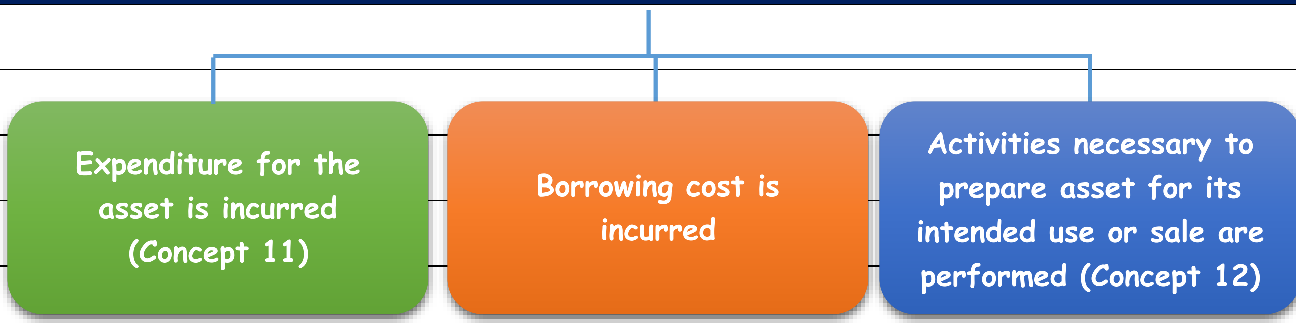
- Capitalisation rate is used to calculate borrowing cost related to qualifying asset.
- Capitalisation rate is the weighted average rate of borrowing cost.
- Amount of borrowing costs capitalized should not exceed actual borrowing cost.

CONCEPT 9 : EXCESS OF THE CARRYING AMOUNT OVER RECOVERABLE AMOUNT

- When the carrying amount or the expected ultimate cost of the qualifying asset exceeds its recoverable amount or net realisable value, the carrying amount is written down or written off in accordance with the requirements of other Standards.
- In certain circumstances, the amount of the write-down or write-off is written back in accordance with those other Standards.

CONCEPT 10 : COMMENCEMENT OF CAPITALISATION OF BORROWING COST

[3 Conditions]



CONCEPT 11 : EXPENDITURE INCURRED ON QUALIFYING ASSET

Sr. No	Particulars	Rs.
i)	Cash payments made during the year	xx
ii)	Transfer of assets during the year	xx
iii)	Assumption of interest bearing liabilities	xx
iv)	Less : Progress payments received	(xx)
v)	Less : Government Grants received (Ind AS 20)	(xx)
vi)	Expenditure incurred	xx

CONCEPT 12 : ACTIVITIES NECESSARY TO PREPARE ASSET

Includes

Technical & administrative work prior to the commencement of physical construction

Excludes

Holding of asset when no production or development takes place that changes asset's condition

Example : Borrowing costs incurred while land is under development are capitalised during the period in which activities related to development are undertaken. However, borrowing costs incurred while land acquired for building purposes is held without any development activity do not qualify for capitalisation.

CONCEPT 13 : SUSPENSION OF CAPITALISATION

Suspended

[1] When active development is interrupted.

Not Suspended

[1] When substantial technical & administrative work is carried out.
[2] When temporary delay is necessary to make the asset ready for its intended use & sale.

Example : Capitalisation continues during extended period that high water levels delay construction of a bridge, if such high water levels are common during construction period in geographical region involved.

CONCEPT 14 : CESSATION OF CAPITALISATION

- When substantially all the activities necessary to prepare qualifying asset are completed.
- Asset is normally ready for its intended use or sale when physical construction of asset is complete even though routine administrative work might still continue.
- If minor modifications are outstanding, it indicates that substantially all the activities are complete.
  - Eg : Decoration of a property to the purchaser's or user's specification.
- When construction of qualifying asset is in parts & completed part is ready to use.

Example :

1. Business park with several buildings, each of which can be used individually, is an example of qualifying asset for which each part is capable of being used while construction continues on other parts.
2. On the other side, in case of an industrial undertaking such as steel mill, all parts have to be completed before any completed part can be put to use.

CONCEPT 15 : DISCLOSURES

1. Accounting Policy adopted for borrowing cost.
2. Amount of borrowing cost capitalized during the period.