IFRS Accounting Standards discussion fora:
IAS 23 *Borrowing Costs*

2023
Addis Ababa, Ethiopia

Accounting and Audit Board of Ethiopia
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Aims

» Develop a more cohesive understanding of IFRS accounting and reporting for borrowing costs in Ethiopia

» Enhance capacity in Ethiopia to apply IAS 23 *Borrowing Costs* more consistently

Applicable version of IFRS Accounting Standards

Unless specified otherwise, the accounting requirements that are the subject matter of this discussion forum are IFRS Accounting Standards as issued by the International Accounting Standards Board that are applicable for annual period beginning on or after 1 January 2023 without early applying new and amended IFRS Accounting Standards that have a later mandatory application date.

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Issue 1: Foreign loans

Foreign loans
What do you think?

IAS 23 *Borrowing costs* requires the capitalisation of borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset.[1]

With respect to qualifying borrowing cost, IAS 23 allows capitalization of foreign exchange losses from interest rate qualifying differences between the foreign and local banks for similar loans. We use effective interest rate to calculate all these. What should we do if the effective rate is not available? How similar should the comparative loans be?

[1] IAS 23.1

Foreign loans
Summary of discussion

With respect to qualifying borrowing cost, IAS 23 allows capitalization of foreign exchange losses from interest rate differences between the foreign and local banks for similar loans. We use effective interest rate to calculate all these. What should we do if the effective rate is not available? How similar should the comparative loans be?

Discussants' consensus view:

» IAS 23.11 notes judgement is involved in determining the appropriate rate when the loan is denominated in a foreign currency[1]

» The objective of IAS 23 is to capitalize the interest rate component of the change in exchange rate over the period

[1] See also IFRIC Agenda decision, Foreign Exchange and capitalizable borrowing costs, January 2008

Foreign loans
Summary of discussion *continued*

What should we do if the effective rate is not available? How similar should the comparative loans be?

Discussants' consensus view *continued*:

This requires an entity to analyse:

» Interest rate that would have been paid if borrowed in local currency, and

» The interest rate actually paid in the foreign currency

Economically, the change in exchange rate compensates for this difference in interest rates

» Any other change in the exchange rate relates to other factors, and is not relevant for capitalisation

Borrowing costs – foreign loans
Summary of discussion *continued*

What should we do if the effective rate is not available? How similar should the comparative loans be?

Discussants' consensus view *continued*:

To do this:

» The entity has the actual interest rate it has paid on the foreign loan

» It must estimate the interest it would have paid on the domestic loan

Judgment is needed, commonly the estimate can be based on :

» Similar loans the entity has taken

» Quotes the entity received when considering finance alternatives for similar loans

» Similar loans taken by competitors with a similar credit rating

Issue 2: Extended borrowing period

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Extended borrowing period
What do you think?

IAS 23 *Borrowing Costs* requires the capitalisation of borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset.[1]

For borrowing cost on qualifying assets (construction in progress), if construction period is extended and loan is not repaid periodically. How can we treat the capitalisation of the borrowing cost?

[1] IAS 23.1

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Extended borrowing period
Summary of discussion

For borrowing cost on qualifying assets (construction in progress), if construction period is extended and loan is not repaid periodically. How can we treat the capitalisation of the borrowing cost?

Discussants' consensus view

» IAS23.20 requires that entity suspend borrowing costs during extended periods in which it suspends active construction of the asset

» Applying this requirement:

  » If activity is paused on a portion of a development, then capitalisation should be suspended on that portion

  » If activity is ‘materially’ paused (only insignificant work is being done), then capitalisation should be paused