

IAS 16 — Property, Plant and Equipment

Objective of IAS 16

The objective of IAS 16 is to prescribe the accounting treatment for property, plant, and equipment. The principal issues are the recognition of assets, the determination of their carrying amounts, and the depreciation charges and impairment losses to be recognised in relation to them.

Scope

IAS 16 does not apply to

- assets classified as held for sale in accordance with *IFRS 5*
- exploration and evaluation assets (*IFRS 6*)
- biological assets related to agricultural activity (see *IAS 41*) or
- mineral rights and mineral reserves such as oil, natural gas and similar non-regenerative resources

The standard does apply to property, plant, and equipment used to develop or maintain the last two categories of assets. [IAS 16.3]

Recognition

Items of property, plant, and equipment should be recognised as assets when it is probable that: [IAS 16.7]

- it is probable that the future economic benefits associated with the asset will flow to the entity, and
- the cost of the asset can be measured reliably.

This recognition principle is applied to all property, plant, and equipment costs at the time they are incurred. These costs include costs incurred initially to acquire or construct an item of property, plant and equipment and costs incurred subsequently to add to, replace part of, or service it.

IAS 16 does not prescribe the unit of measure for recognition – what constitutes an item of property, plant, and equipment. [IAS 16.9] Note, however, that if the cost model is used (see below) each part of an item of property, plant, and equipment with a cost that is significant in relation to the total cost of the item must be depreciated separately. [IAS 16.43]

IAS 16 recognises that parts of some items of property, plant, and equipment may require replacement at regular intervals. The carrying amount of an item of property, plant, and equipment will include the cost of replacing the part of such an item when that cost is incurred if the recognition criteria (future benefits and measurement reliability) are met. The carrying amount of those parts that are replaced is derecognised in accordance with the derecognition provisions of IAS 16.67-72. [IAS 16.13]

Also, continued operation of an item of property, plant, and equipment (for example, an aircraft) may require regular major inspections for faults regardless of whether parts of the item are replaced. When each major inspection is performed, its cost is recognised in the carrying amount of the item of property, plant, and equipment as a replacement if the recognition criteria are satisfied. If necessary, the estimated cost of a future similar inspection may be used as an indication of what the cost of the existing inspection component was when the item was acquired or constructed. [IAS 16.14]

Initial measurement

An item of property, plant and equipment should initially be recorded at cost. [IAS 16.15] Cost includes all costs necessary to bring the asset to working condition for its intended use. This would include not only its original purchase price but also costs of site preparation, delivery and handling, installation, related professional fees for architects and engineers, and the estimated cost of dismantling and removing the asset and restoring the site (see [IAS 37 Provisions, Contingent Liabilities and Contingent Assets](#)). [IAS 16.16-17]

If payment for an item of property, plant, and equipment is deferred, interest at a market rate must be recognised or imputed. [IAS 16.23]

If an asset is acquired in exchange for another asset (whether similar or dissimilar in nature), the cost will be measured at the fair value unless (a) the exchange transaction lacks commercial substance or (b) the fair value of neither the asset received nor the asset given up is reliably measurable. If the acquired item is not measured at fair value, its cost is measured at the carrying amount of the asset given up. [IAS 16.24]

Measurement subsequent to initial recognition

IAS 16 permits two accounting models:

- o **Cost model.** The asset is carried at cost less accumulated depreciation and impairment. [IAS 16.30]
- o **Revaluation model.** The asset is carried at a revalued amount, being its fair value at the date of revaluation less subsequent depreciation and impairment, provided that fair value can be measured reliably. [IAS 16.31]

The revaluation model

Under the revaluation model, revaluations should be carried out regularly, so that the carrying amount of an asset does not differ materially from its fair value at the balance sheet date. [IAS 16.31]

If an item is revalued, the entire class of assets to which that asset belongs should be revalued. [IAS 16.36]

Revalued assets are depreciated in the same way as under the cost model (see below).

If a revaluation results in an increase in value, it should be credited to other comprehensive income and accumulated in equity under the heading "revaluation surplus" unless it represents the reversal of a revaluation decrease of the same asset previously recognised as an expense, in which case it should be recognised in profit or loss. [IAS 16.39]

A decrease arising as a result of a revaluation should be recognised as an expense to the extent that it exceeds any amount previously credited to the revaluation surplus relating to the same asset. [IAS 16.40]

When a revalued asset is disposed of, any revaluation surplus may be transferred directly to retained earnings, or it may be left in equity under the heading revaluation surplus. The transfer to retained earnings should not be made through profit or loss. [IAS 16.41]

Depreciation (cost and revaluation models)

For all depreciable assets:

The depreciable amount (cost less residual value) should be allocated on a systematic basis over the asset's useful life [IAS 16.50].

The residual value and the useful life of an asset should be reviewed at least at each financial year-end and, if expectations differ from previous estimates, any change is accounted for prospectively as a change in estimate under IAS 8. [IAS 16.51]

The depreciation method used should reflect the pattern in which the asset's economic benefits are consumed by the entity [IAS 16.60];

The depreciation method should be reviewed at least annually and, if the pattern of consumption of benefits has changed, the depreciation method should be changed prospectively as a change in estimate under IAS 8. [IAS 16.61]

Depreciation should be charged to profit or loss, unless it is included in the carrying amount of another asset [IAS 16.48].

Depreciation begins when the asset is available for use and continues until the asset is derecognised, even if it is idle. [IAS 16.55]

Recoverability of the carrying amount

[IAS 36](#) requires impairment testing and, if necessary, recognition for property, plant, and equipment. An item of property, plant, or equipment shall not be carried at more than recoverable amount. Recoverable amount is the higher of an asset's fair value less costs to sell and its value in use.

Any claim for compensation from third parties for impairment is included in profit or loss when the claim becomes receivable. [IAS 16.65]

Derecognition (retirements and disposals)

An asset should be removed from the statement of financial position on disposal or when it is withdrawn from use and no future economic benefits are expected from its disposal. The gain or loss on disposal is the difference between the proceeds and the carrying amount and should be recognised in profit and loss. [IAS 16.67-71]

If an entity rents some assets and then ceases to rent them, the assets should be transferred to inventories at their carrying amounts as they become held for sale in the ordinary course of business. [IAS 16.68A]

Disclosure

For each class of property, plant, and equipment, disclose: [IAS 16.73]

- o basis for measuring carrying amount
- o depreciation method(s) used

- o useful lives or depreciation rates
- o gross carrying amount and accumulated depreciation and impairment losses
- o reconciliation of the carrying amount at the beginning and the end of the period, showing:

- o additions
- o disposals
- o acquisitions through business combinations
- o revaluation increases or decreases
- o impairment losses
- o reversals of impairment losses
- o depreciation
- o net foreign exchange differences on translation
- o other movements

Also disclose: [IAS 16.74]

- o restrictions on title
- o expenditures to construct property, plant, and equipment during the period
- o contractual commitments to acquire property, plant, and equipment
- o compensation from third parties for items of property, plant, and equipment that were impaired, lost or given up that is included in profit or loss

If property, plant, and equipment is stated at revalued amounts, certain additional disclosures are required: [IAS 16.77]

- o the effective date of the revaluation
- o whether an independent valuer was involved
- o the methods and significant assumptions used in estimating fair values
- o the extent to which fair values were determined directly by reference to observable prices in an active market or recent market transactions on arm's length terms or were estimated using other valuation techniques
- o for each revalued class of property, the carrying amount that would have been recognised had the assets been carried under the cost model
- o the revaluation surplus, including changes during the period and any restrictions on the distribution of the balance to shareholders

IFRS 5 — Non-current Assets Held for Sale and Discontinued Operations

Background

IFRS 5 achieves substantial convergence with the requirements of [US SFAS 144 Accounting for the Impairment or Disposal of Long-Lived Assets](#) with respect to the timing of the classification of operations as discontinued operations and the presentation of such operations. With respect to long-lived assets that are not being disposed of, the impairment recognition and measurement standards in SFAS 144 are significantly different from those in IAS 36 Impairment of Assets. However those differences have not been addressed in the short-term convergence project.

Key provisions of IFRS 5 relating to assets held for sale

Held-for-sale classification. In general, the following conditions must be met for an asset (or 'disposal group') to be classified as held for sale: [IFRS 5.6-8]

- o management is committed to a plan to sell
- o the asset is available for immediate sale
- o an active programme to locate a buyer is initiated
- o the sale is highly probable, within 12 months of classification as held for sale (subject to limited exceptions)
- o the asset is being actively marketed for sale at a sales price reasonable in relation to its fair value
- o actions required to complete the plan indicate that it is unlikely that plan will be significantly changed or withdrawn

The assets need to be disposed of through sale. Therefore, operations that are expected to be wound down or abandoned would not meet the definition (but may be classified as discontinued once abandoned). [IFRS 5.13]

However, all classification, presentation and measurement requirements of IFRS 5 apply to a non-current asset (or disposal group) that is classified as held for distribution to owners. [IFRS 5.5A and IFRIC 17]

Disposal group. A 'disposal group' is a group of assets, possibly with some associated liabilities, which an entity intends to dispose of in a single transaction. The measurement basis required for non-current assets classified as held for sale is applied to the group as a whole, and any resulting impairment loss reduces the carrying amount of the non-current assets in the disposal group in the order of allocation required by IAS 36. [IFRS 5.4]

Measurement. The following principles apply:

- o *At the time of classification as held for sale.* Immediately before the initial classification of the asset as held for sale, the carrying amount of the asset will be measured in accordance with applicable IFRSs. Resulting adjustments are also recognised in accordance with applicable IFRSs. [IFRS 5.18]
- o *After classification as held for sale.* Non-current assets or disposal groups that are classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell. [IFRS 5.15]
- o *Impairment.* Impairment must be considered both at the time of classification as held for sale and subsequently:
 - o *At the time of classification as held for sale.* Immediately prior to classifying an asset or disposal group as held for sale, measure and recognise impairment in accordance with the applicable IFRSs (generally IAS 16, IAS 36, IAS 38, and IAS 39). Any impairment loss is recognised in profit or loss unless the asset had been measured at revalued amount under IAS 16 or IAS 38, in which case the impairment is treated as a revaluation decrease.
 - o *After classification as held for sale.* Calculate any impairment loss based on the difference between the adjusted carrying amounts of the asset/disposal group and fair value less costs to sell. Any impairment loss that arises by using the measurement principles in IFRS 5 must be recognised in profit or loss (IFRS 5.20), even for assets previously carried at revalued amounts. This is supported by IFRS 5 BC.47 and BC.48, which indicate the inconsistency with IAS 36.
- o *Assets carried at fair value prior to initial classification.* For such assets, the requirement to deduct costs to sell from fair value will result in an immediate charge to profit or loss.
- o *Subsequent increases in fair value.* A gain for any subsequent increase in fair value less costs to sell of an asset can be recognised in the profit or loss to the extent that it is not in excess of the cumulative impairment loss that has been recognised in accordance with IFRS 5 or previously in accordance with IAS 36. [IFRS 5.21-22]

Non-depreciation. Non-current assets or disposal groups that are classified as held for sale shall not be depreciated. [IFRS 5.25]

Balance sheet presentation. Assets classified as held for sale, and the assets and liabilities included within a disposal group classified as held for sale, must be presented separately on the face of the balance sheet (statement of financial position). [IFRS 5.38]

Disclosures. [IFRS 5.41]

- o description of the non-current asset or disposal group
- o description of facts and circumstances of the sale (disposal) and the expected timing
- o impairment losses and reversals, if any, and where in the statement of comprehensive income they are recognised
- o if applicable, the reportable segment in which the non-current asset (or disposal group) is presented in accordance with [IFRS 8](#)

8 Operating Segments

Subsidiaries Held for Disposal

IFRS 5 applies to accounting for an investment in a subsidiary for which control is intended to be temporary because the subsidiary was acquired and is held exclusively with a view to its subsequent disposal in the near future. For such a subsidiary, if it is highly probable that the sale will be completed within 12 months then the parent should account for its investment in the subsidiary under IFRS 5 as an asset held for sale, rather than consolidate it under IAS 27.

However, IAS 27 still requires that if a subsidiary that had previously been consolidated is now being held for sale, the parent must continue to consolidate such a subsidiary until it is actually disposed of. It is not excluded from consolidation and reported as an asset held for sale under IFRS 5.

An entity that is committed to a sale involving loss of control of a subsidiary that qualifies for held-for-sale classification under IFRS 5 shall classify all of the assets and liabilities of that subsidiary as held for sale, even if the entity will retain a non-controlling interest in its former subsidiary after the sale.

Key provisions of IFRS 5 relating to discontinued operations

Classification as discontinuing. A discontinued operation is a component of an entity that either has been disposed of or is classified as held for sale, and: [IFRS 5.32]

- o represents either a separate major line of business or a geographical area of operations, and
- o is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations, or
- o is a subsidiary acquired exclusively with a view to resale and the disposal involves loss of control.

Income statement presentation. The sum of the post-tax profit or loss of the discontinued operation and the post-tax gain or loss recognised on the measurement to fair value less cost to sell or fair value adjustments on the disposal of the assets (or disposal group) should be presented as a single amount on the face of the statement of comprehensive income. If the entity presents profit or loss in a separate income statement, a section identified as relating to discontinued operations is presented in that separate statement. [IFRS 5.33-33A].

Detailed disclosure of revenue, expenses, pre-tax profit or loss and related income taxes is required either in the notes or in the statement of comprehensive income in a section distinct from continuing operations. [IFRS 5.33] Such detailed disclosures must cover both the current and all prior periods presented in the financial statements. [IFRS 5.34]

Cash flow statement presentation. The net cash flows attributable to the operating, investing, and financing activities of a discontinued operation shall be separately presented on the face of the cash flow statement or disclosed in the notes. [IFRS 5.33]

No retroactive classification. IFRS 5 prohibits the retroactive classification as a discontinued operation, when the discontinued criteria are met after the balance sheet date. [IFRS 5.12]

Disclosures.

In addition to the income statement and cash flow statement presentations noted above, the following disclosures are required:

- o adjustments made in the current period to amounts disclosed as a discontinued operation in prior periods must be separately disclosed. [IFRS 5.35]
- o if an entity ceases to classify a component as held for sale, the results of that component previously presented in discontinued operations must be reclassified and included in income from continuing operations for all periods presented. [IFRS 5.36]

IAS 23 — Borrowing Costs

Objective of IAS 23

The objective of IAS 23 is to prescribe the accounting treatment for borrowing costs. Borrowing costs include interest on bank overdrafts and borrowings, amortisation of discounts or premiums on borrowings, finance charges on finance leases and exchange differences on foreign currency borrowings where they are regarded as an adjustment to interest costs.

Key definitions

Borrowing cost may include: [IAS 23.6]

- o interest expense calculated by the *effective interest method under IAS 39*,
- o finance charges in respect of finance leases recognised in accordance with IAS 17 Leases, and
- o exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs

This standard does not deal with the actual or imputed cost of equity, including any preferred capital not classified as a liability pursuant to [IAS 32](#). [IAS 23.3]

A **qualifying asset** is an asset that takes a substantial period of time to get ready for its intended use or sale. [IAS 23.5] That could be property, plant, and equipment and investment property during the construction period, intangible assets during the development period, or "made-to-order" inventories. [IAS 23.6]

Scope of IAS 23

Two types of assets that would *otherwise be qualifying assets* are *excluded* from the scope of IAS 23:

- o qualifying assets measured at fair value, such as biological assets accounted for under IAS 41 Agriculture
- o inventories that are manufactured, or otherwise produced, in large quantities on a repetitive basis and that take a substantial period to get ready for sale (for example, maturing whisky)

Accounting treatment

Recognition

Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset form part of the cost of that asset and, therefore, should be capitalised. Other borrowing costs are recognised as an expense. [IAS 23.8]

Measurement

Where funds are borrowed specifically, costs eligible for capitalisation are the actual costs incurred less any income earned on the temporary investment of such borrowings. [IAS 23.12] Where funds are part of a general pool, the eligible amount is determined by applying a capitalisation rate to the expenditure on that asset. The capitalisation rate will be the weighted average of the borrowing costs applicable to the general pool. [IAS 23.14]

Capitalisation should commence when expenditures are being incurred, borrowing costs are being incurred and activities that are necessary to prepare the asset for its intended use or sale are in progress (may include some activities prior to commencement of physical production). [IAS 23.17-18] Capitalisation should be suspended during periods in which active development is interrupted. [IAS 23.20] Capitalisation should cease when substantially all of the activities necessary to prepare the asset for its intended use or sale are complete. [IAS 23.22] If only minor modifications are outstanding, this indicates that substantially all of the activities are complete. [IAS 23.23]

Where construction is completed in stages, which can be used while construction of the other parts continues, capitalisation of attributable borrowing costs should cease when substantially all of the activities necessary to prepare that part for its intended use or sale are complete. [IAS 23.24]

Disclosure [IAS 23.26]

- o amount of borrowing cost capitalised during the period
- o capitalisation rate used