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AS - 16
Borrowing Costs

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044 2814 2616 / 3296 4602

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Borrowing Cost

Interest and other cost incurred by an enterprise in connection with the borrowing of funds

Example for Other cost: Amortization of discounts or premiums relating to borrowings

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What is a Qualifying Asset?

An asset that necessarily takes a substantial period of time to get ready for its intended use or sale

Examples: Manufacturing plants, construction of building etc.

Substantial period primarily depends on the facts and circumstances of each case. However, ordinarily, a period of twelve months is considered as substantial period of time unless a shorter or longer period can be justified on the basis of facts and circumstances of the case.

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As per AS 16, Borrowing costs incurred on constructing or acquiring a qualifying asset, is capitalized as cost of that asset.

All other Borrowing costs are charged to P&L Account.

When Capitalisation shall Commence?

The capitalization of borrowing costs should commence when all the following conditions are satisfied:

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Expenditure for the acquisition, construction or production of a qualifying asset is being incurred;

Borrowing costs are being incurred

Activities that are necessary to prepare the asset for its intended use or sale are in progress.

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When Capitalisation shall be suspended?

Borrowing costs may be incurred during an extended period in which the activities necessary to prepare an asset for its intended use or sale are interrupted. Such costs are costs of holding partially completed assets and do not qualify for capitalization.

However, capitalization of borrowing costs is not normally suspended during a period when substantial technical and administrative work is being carried out. Capitalisation of borrowing costs is also not suspended when a temporary delay is a necessary part of the process of getting an asset ready for its intended use or sale.

For example, capitalization continues during the extended period needed for inventories to mature or the extended period during which high water levels delay construction of a bridge, if such high water levels are common during the construction period in the geographic region involved.

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When Capitalisation shall be ceased?

Capitalisation of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.

When the construction of a qualifying asset is completed in parts and a completed part is capable of being used while construction continues for the other parts, capitalization of borrowing costs in relation to a part should cease when substantially all the activities necessary to prepare that part for its intended use or sale are complete.

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Capitalisation for different types of Borrowing

Specific Borrowing

Treatment:

Actual Borrowing
Less: Income from Temporary Investment

General Borrowing

Treatment:

Apply capitalization rate to the Expenditure on that asset. *The capitalization rate should be the weighted average of the borrowing costs applicable to the borrowings of the enterprise that are outstanding during the period,*

Note

The amount of borrowing costs capitalised during the period should not exceed the amount of borrowing costs incurred during the period.