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| FRD 105 |  |  | Borrowing costs (April 2022) |
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| Purpose |  | 1.1 | To prescribe the requirements for the treatment of ‘borrowing costs.’ |
| Application |  | **2.1** | Applies to all entities defined as either a public body or a department under section 3 of the *Financial Management Act* *1994*, except those entities which are not controlled by the State and whose financial position and result are thus not included in the Annual *Financial Report for the State of Victoria*. Application by those exempted entities and by State owned corporations is encouraged. |
| Operative date |  | **3.1** | Annual reporting periods commencing on or after 1 July 2015. |
|  |  | **3.2** | FRD 105B *Borrowing costs* is renamed to FRD 105 *Borrowing costs* effective 1 April 2022. |
| Requirements |  | **4.1** | ‘Not-for-profit’ entities  Entities that are classified as ‘not-for-profit’ entities shall expense all borrowing costs in the period in which they are incurred. |
|  |  | **4.2** | ‘For-profit’ entities  Entities that are classified as ‘for-profit’ entities shall account for borrowing costs in accordance with the requirements of AASB 123 *Borrowing Costs*. |
|  |  | **4.3** | In addition, for each reporting period, ‘for-profit’ entities whose qualifying assets include capitalised borrowing costs shall advise the Department of Treasury and Finance’s Consolidated Reporting and Analysis team of the relevant cumulative and current period adjustments to their financial results and position for the purpose of consolidation into the Annual *Financial Report for the State of Victoria* on a not-for-profit basis. |
| Definitions |  | 5.1 | Refer to paragraph 5 of AASB 123 for the following definitions:  borrowing costs; and  qualifying assets. |
| Guidance |  | 6.1 | ‘Not-for-profit’ entities  This Financial Reporting Direction (FRD) continues the requirement that applicable entities recognise borrowing costs as an expense in the period in which they are incurred, regardless of how the borrowings are applied, as allowed by AASB 123, for ‘not-for-profit’ public sector entities. |
|  |  | 6.2 | This maintains consistency with the rules and principles of the ABS Government Finance Statistics (GFS) Manual, as required by AASB 1049 *Whole of Government and General Government Sector Financial Reporting*. |
|  |  | 6.3 | **‘For-profit’ entities**  FRD 108 *Classification of Entities as For-Profit* identifies the public bodies that are classified as ‘for-profit’. |
|  |  | 6.4 | The election to recognise borrowing costs as an expense is not available to ‘for-profit’ public sector entities from 1 July 2009. Such entities will need to capitalise their borrowing costs that are directly attributable to the acquisition, construction, or production of a qualifying asset, as part of the cost of that asset, as required by AASB 123. |
|  |  | 6.5 | However, AASB 123 paragraph 4(a) does provide an exception, whereby an entity is not required to apply AASB 123 to borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset measured at fair value. |
|  |  | 6.6 | AASB 10 *Consolidated Financial Statements* requires uniform accounting policies to be used when preparing consolidated financial statements, which includes the Annual *Financial Report for the State of Victoria* (AFR). Accordingly, ‘for-profit’ public sector entities whose qualifying assets include capitalised borrowing costs shall advise the Department of Treasury and Finance’s Consolidated Reporting and Analysis team of the appropriate cumulative and current period adjustments to their financial results and position for the purpose of consolidation into the AFR on a ‘not-for-profit’ basis. |
|  |  | 6.7 | AASB 123 scopes out qualifying assets measured at fair value. Consequently, where assets have been revalued to fair value subsequent to construction/acquisition, the adjustment to fair value is deemed to have eliminated any capitalisation of borrowing costs. |
| Relevant pronouncements |  | 7.1 | AASB 101 *Presentation of Financial Statements*  AASB 123 *Borrowing Costs*  AASB 1049 *Whole of Government and General Government Sector Financial Reporting*  FRD 103 *Non-financial physical assets*  FRD 108 *Classification of entities as for-profit* |
| Background |  | 8.1 | FRD 105 reflected the earlier AASB 123, which required the immediate expensing of borrowing costs, but allowed the capitalisation of borrowing costs directly attributable to the acquisition, construction or production of a *qualifying asset* as an alternative treatment.  Expensing of borrowing costs was determined to be the most appropriate treatment to provide consistency across government and to improve convergence with the Government Finance Statistics framework.  A later amendment to AASB 123 (14 Jun 2007) prescribed entities to capitalise their borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset, as part of the cost of that asset. However, it allows a ‘not-for-profit’ public sector entity to continue the election to recognise borrowing costs as an expense in the period in which they are incurred regardless of how the borrowings are applied (AASB 123 paragraph Aus8.1)  The expensing option is not extended to the ‘for-profit’ public sector entities except where the borrowing costs are directly attributable to the acquisition, construction or production of a qualifying asset measured at fair value (AASB 123 paragraph 4a). Accordingly, FRD 105 was revised to reflect this change for “for-profit” public sector entities, as listed in FRD 108. |
|  |  | 8.2 | This FRD was revised in:  June 2016 to remove first-time adoption requirements as they are no longer required. The ‘Disclosure within the Model Report for Victorian Government Departments’ section was also removed as this disclosure has been included in the *Model Report for Victorian Government Departments*. |