

UKSIP

The Society of Investment Professionals

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Accounting Standards Board

Dear Sirs

Re FRED 29: Inventories, Construction and Service Contracts

I attach the Society's response to the above exposure draft.

Please note that we have separated our comments between ASB questions and IASB questions. While we are content for our responses to ASB questions to be made available publicly, we request that our responses to the IASB question remain confidential.

Yours faithfully

Paul H Richards

Property, plant and equipment; Borrowing costs (FRED 29) issued by the Accounting Standards Board

ASB(i) Do you agree with the proposal to issue new UK standards on property, plant and equipment and borrowing costs when the IASB issues the revised IAS 16, unless it becomes clear that further changes to IAS 16 are likely by 2005 as a result of the revaluation project?

Yes.

ASB(ii) The international exposure draft on property, plant and equipment proposes that residual values used in the calculation of depreciable amount should be reviewed at each balance sheet date and revised to reflect current estimates. FRS 15 generally requires prices at the date of acquisition or latest valuation to be used; hence, depreciation expense on a historical cost basis is not reduced by inflation in residual values. Do you agree or disagree with the proposed international approach?

The Society supports the international approach.

ASB(iii) IAS 16 does not address the use of renewals accounting in respect of certain infrastructure assets. Do you believe that the absence of the guidance in FRS 15 would prevent entities from using renewals accounting as a method of estimating depreciation? Should UK entities be permitted to continue to use renewals accounting?

Renewals accounting should not be permitted.

ASB(iv) What are your views on the differences between the requirements of FRS 15 and IAS 16 concerning revaluations (as described in paragraphs 10 to 17 of the Preface to the FRED)?

The Society supports the application of market values for all assets not just those which are surplus.

ASB(v) Are there any other aspects of the differences between the proposed standards and current UK accounting requirements that you wish to comment on?

Guidance should be provided to accounts preparers along the lines indicated in paragraph 16 on page 9 of the exposure draft. Guidance is an important part of the underlying accounting standard.

ASB(vi) Do you agree with the ASB's proposal, as a transitional measure (see paragraph 18 above), that the present exemption in FRS 15 in respect of insurance companies should be retained in a new UK standard based on IAS 16 revised pending the outcome of the IASB's projects on insurance and reporting financial performance?

Yes.

ASB(vii) The transitional arrangements for the first-time application of FRS 15 allowed an entity that does not adopt a policy of revaluation to retain carrying amounts reflecting previous revaluations instead of restating the carrying amounts to historical cost (see paragraph 19 above). Do you believe that a transitional arrangement should be included in a new UK standard to allow entities that adopted FRS 15's transitional arrangement to continue to recognise the carrying amounts under that arrangement?

No.

ASB(viii) Do you believe that ASB should consider any other transitional arrangements?

No.

ASB(ix) Are there any other aspects of the draft standard on property, plant and equipment that the ASB should request the IASB to review when finalising the revised IAS 16?

No.

ASB(x) Do you agree that the capitalisation of borrowing costs should remain optional? If you had to choose between mandatory capitalisation and prohibition of capitalisation, which would you support and why?

There should not be a choice of accounting treatment. The Society does not agree that capitalisation of borrowing costs should be permitted and therefore supports a prohibition of capitalisation. Interest costs incurred by a company must be expensed. The argument in favour of capitalisation is based on a comparison of the situation of the company developing its own property and that of acquiring a developed property from a developer. The Society considers these to be different situations and that where interest is incurred it should be expensed. Any profit arising from the difference between the cost and the value of the property developed by the company can be addressed under the valuation of property.

ASB(xi) Do you agree that paragraph 5(e) of IAS 23, which allows certain exchange differences to be capitalised, should be deleted in the draft standard on borrowing costs?

Yes. It is this type of accounting treatment which enabled Polly Peck to mislead investors. Capitalisation should not be permitted in any circumstances.

ASB(xii) What are your views on the difference between IAS 23 and FRS 15 referred to in paragraph 24 of the Preface to the FRED concerning borrowing costs eligible for capitalisation?

See our comments above.

ASB(xiii) Do you have any comments on IAS 23 that you wish the ASB to bring to the IASB's attention?

Fair values should be used as the basis for valuation.

FRED 29: IASB questions

(UKSIP response to remain confidential)

IASB(i) Do you agree that all exchanges of items of property, plant and equipment should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably (see paragraphs 21 and 21A of the [draft] FRS on property, plant and equipment)?

Yes.

IASB(ii) Do you agree that all exchanges of intangible assets should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably?

Yes.

IASB(iii) Do you agree that depreciation of an item of property, plant and equipment should not cease when it becomes temporarily idle or is retired from active use and held for disposal (see paragraph 59 of the [draft] FRS on property, plant and equipment)?

The Society agrees.

REF: Fred 29/205/Sept/02