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26 September 2002

Hans Nailor
Accounting Standards Board,
Holborn Hall,
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London WC1X 8AL

Fred29@asb.org.uk

Dear Mr Nailor,

Exposure draft: FRED 29 Property, plant and equipment

I am writing in response to the invitation to comment on Exposure Draft FRED 29: Property, plant and equipment; Borrowing costs. I appreciate that this response is after the deadline given in the exposure draft but hope that my views are still useful to you.

My answers to the questions posed in the Exposure Draft are set out in the accompanying appendix. From these you will see that my main concern is around the uncertainty on revaluation policy. I consider the policy in FRS 15 to be superior to that in IAS 16. Assuming that no immediate change is forthcoming here for IAS 16, I believe that the ASB should hold back in issuing FRS 15 (revised). To adopt the IAS 16 policy before 2005 weakens our position and imposes an inferior result on the UK constituency earlier than necessary.

Yours sincerely,

Alison Bexfield
Technical accounting manager

Appendix

Property, plant and equipment; Borrowing costs (FRED 29)

- 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?

We are in favour of a gradual implementation for changes to UK GAAP where the proposed changes are very straight forward to implement (and hence easy for users of the accounts to understand) or where they are unlikely to have a major effect on the majority of companies. This standard fits within this category for those companies that have opted not to revalue assets as IAS 16 also permits a choice in the matter of revaluation.

But the revaluation issue is one of some significance and FRS 15 also covers those companies that have opted to revalue assets. Currently there are difference in the UK approach to revaluation in FRS 15 and that in IAS 16. I believe that the UK approach is superior to that of IAS 16. For the UK to effectively adopt IAS 16 early (prior to 2005) might be seen as a weakening of our position concerning the revaluation issue. If we truly believe the approach in FRS 15 is superior, then we should continue with it right up to 2005 rather than adopt an 'inferior standard' early.

In light of this, I do support the proposal to issue a revised FRS 15 whilst the position on revaluation remains unclear. Should this issue be resolved with new proposals from the IASB, the resulting proposed changes to FRS 15 will need to be reissued for consultation in the UK.

- 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?

We disagree with the proposed international approach. Under this approach, where a company has chosen not to revalue its assets it will be required to mix historic cost accounting (for the acquisition cost) with current cost accounting (for the residual value) all for the one asset. This does not appear very sensible with the net book value representing neither one basis nor the other.

- 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?

No comment.

- 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)?

We prefer the existing UK approach to revaluations within FRS 15 than that set out in IAS 16. In particular we do not agree with the IAS 16 approach whereby a property could be revalued upwards to reflect a high open market value in a situation where the company concerned requires the property to be used within its business and has no intention of selling it. In such a case, the higher market value should merely be indicated in the notes to the accounts as is required by FRS 15.

The IAS 16 approach would take the accounts another step away from the reality of how management operate their business. We prepare accounts on a going concern basis, and tangible fixed assets represent assets for ongoing use in the business. Valuing assets at a higher open market value would take no account of the disruption to the business of selling up and moving operations to another site or the unlikelihood of this occurring. It could also result in spurious revaluation gains in the performance statement that are unlikely to be realised and that may mislead users of the accounts.

- 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?

No.

- 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?

No comment.

- 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?

Yes. We believe a similar transitional arrangement should be included. This is a pragmatic arrangement so that companies do not incur undue burdens when adopting the new standard. Over time any differences are eliminated as the assets concerned reach the end of their useful lives.

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

As already stated, I believe that the ASB should hold back on issuing a revised FRS 15 whilst the revaluation debate is ongoing. The ASB should not adopt an inferior standard in the UK earlier than is required for 2005 harmonisation.

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?

The revised IAS 16 has fewer regulations governing revaluations than FRS 15. It might be sensible for it to include a maximum period, as FRS 15 currently does, after which a full revaluation is required for companies that have adopted the revaluation option.

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?

We agree this should remain optional until the subject has been properly debated.

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?

No. This is a new stand alone standard for the UK. It would therefore be sensible for it to mirror IAS 23. This is not a principle where I feel the ASB needs to take a stand.

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?

No comment

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

No.

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The IASB has asked commentators to respond to the following questions on the

proposed changes to IAS 16:

- 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?

No comment.

- 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 simple example of a car illustrates how an asset continues to depreciate in value, due to its age, even when not being used. So it appears sensible to continue with depreciation of the asset. However, residual values may change and the rate of depreciation might change once the asset is taken out of use. Such changes are permitted by the standard and so I have no problem with continuing to depreciate in such circumstances.

16 September 2002

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Dear Mr Nailor,

Exposure draft: FRED 27 Events after the balance sheet date

I am writing in response to the invitation to comment on Exposure Draft FRED 27: events after the balance sheet date.

We support the changes proposed in FRED 27. It is sensible to bring this standard fully in line with FRS 12 once UK law has been amended to permit this.

Yours sincerely,

Alison Bexfield
Technical accounting manager

