



## **Comment on Exposure Draft titled Property, Plant and Equipment –**

### **Proceeds before Intended Use (Amendments to Ind AS 16)**

Thank you so much for the opportunity to comment on the exposure draft of Ind AS 16, Property, Plant and Equipment, titled Property, Plant and Equipments: Proceeds before intended use

1. The exposure draft proposes to amend Ind AS 16, *Property, Plant and Equipment*, by prohibiting deduction from the costs of an item of property, plant and equipment any proceeds from selling items produced while bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management and requiring an entity instead, to recognise those sales proceeds as income / revenue in profit or loss. The amendment proposed seems to be more of an anti-abuse measure introduced with a narrow focus and hence narrow analysis has been done without backing the same with sound conceptual basis.
2. Attention is drawn to the requirements of paragraph 12 of Ind AS 23, *Borrowing Costs*, which requires that to determine the amount of borrowing costs eligible for capitalisation, any investment income on the temporary investment of those borrowings shall be deducted from the actual borrowing costs incurred. It may be noted that the income to be deducted could be higher than the borrowing costs incurred. This is because, there is no prohibition as not to deduct the excess of investment income over the borrowing costs incurred. Therefore, the amendment proposed is inconsistent with the requirements of other Ind ASs. The ASB should make a consequential amendment to the requirements of paragraph 12 of Ind AS 23 so as to require recognition of investment income in profit or loss.
3. As per the conceptual framework, income or expense result from changes in assets and liabilities. If the sales proceeds of items produced during testing are recognised as income, there should be corresponding recognition of expense due to consumption of the asset. While producing inventories, not only inventories but also that item of property, plant and equipment is consumed. Generating income / revenue from using an asset without its use being recognised produces misleading information. It is extremely difficult to understand how an entity can generate income / revenue from using an item of property, plant and equipment that is not yet available for use. If the ASB is adamant in going forward with the amendment

proposed, it is a humble request to change the timing of commencement of depreciation to the point of before testing. This will ensure that an entity records consumption of the asset while recognising income / revenue for items produced from that asset. However, preponing the commencement of depreciation could have other unintended consequences.

4. Recognising the cost of items produced during testing as cost of inventories is inconsistent with the cost recognition principles stated in IAS 16. Incurrence of cost of items produced during testing is necessary to test the technical and physical performance of the item of property, plant and equipment. Therefore, the proposed amendment creates inconsistencies not only between standards in Ind AS framework but also within a standard.
5. From the exposure draft, it seems that the discomfort of ASB is with regard to recognising the excess of sales proceeds over costs incurred for items produced during testing in the costs of the item of property, plant and equipment. However, the same discomfort arises from paragraph 12 of Ind AS 23 as stated above. Such a discomfort could have been addressed by requiring such excess to be recognised in profit or loss rather than requiring all sales proceeds be recognised as revenue and cost of items produced as inventories which has uninvited ramifications.
6. Further, it is not clear whether the income generated from selling the items produced during testing will meet the definition of revenue as defined in Ind AS 115, Revenue from Contracts with Customers. Appendix A of Ind AS 115 defines revenue as income arising in the course of an entity's ordinary activities. It is not clear from this definition what does ordinary activities mean. Ind AS 2, Inventories, defines inventories, inter alia, as assets held for sale in the ordinary course of business. A question arises whether ordinary activities used in the definition of revenue mean ordinary course of business used in the definition of inventories. Paragraph 34 of Ind AS 2 provides the answer by requiring inventories to be recognised as expense when the related revenue is recognised. Thus, ordinary activities in Ind AS 115 means ordinary course of business. It may be noted that an item produced from testing an item of property, plant and equipment and selling the same may be an ordinary activity from Ind AS 1, Presentation of Financial Statements, perspective which prohibits presentation as extraordinary items but may not be an item held for sale in the ordinary course of business.



Therefore, it is doubtful whether such income could be regarded as revenue and the item produced as inventory. The ASB is requested to clarify in this regard.

