



## **Issues Resolution Memo No. 89-1**

Issued: June 2018; Implementation: July 2019

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### **BACKGROUND**

GASB issued Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*, to improve financial reporting by providing users of financial statements with more relevant information about capital assets and the cost of borrowing for a reporting period and simplify accounting for interest cost incurred before the end of a construction period.

This Statement establishes accounting requirements for interest cost incurred before the end of a construction period and supersedes the requirements of paragraphs 5-22 of Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*.

This Statement requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred.

This Statement is effective for reporting periods beginning after December 15, 2019. Earlier application is encouraged. The requirements of this Statement should be applied prospectively. The University elected an early adoption of this Statement for reporting period beginning July 1, 2019.

### **DEFINE ISSUES**

The University must determine whether GASB Statement No. 89 changes any existing financial reporting and disclosure requirements for any of the University's financial reporting entities.

### **AUTHORITATIVE GUIDANCE AND APPROACH**

This Statement requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred. Interest cost would not be capitalized as part of the historical cost of a capital asset.

### **IMPLEMENTATION**

Effective July 1, 2019, the University would stop recording capitalized interest and eliminate all year-end closing steps related to capitalized interest.

### **CONCLUSION**

For construction in progress, interest cost incurred after applying this Statement on July 1, 2019 would not be capitalized as part of capital asset. As a result, the University's interest expense would increase upon implementation of the Statement.



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### Addendum to IRM No. 89-1

#### FREQUENTLY ASKED QUESTIONS

- 1. Could the University continue to finance interest cost incurred before the end of a construction period through external financing?**

Yes, there will be no changes on the financing side and the University could continue to fund interest cost through external financing (i.e. commercial paper and bonds).

- 2. How would interest income earned on unspent bond proceeds be reporting on Annual Financial Report?**

*Statements of Net Position* - Interest income earned on unspent bond proceeds would continue to be included as Restricted Expendable under Net Position section.

*Statements of Revenues, Expenses, and Changes in Net Position* - Interest income earned on unspent bond proceeds would continue to be reported as Investment Income under Nonoperating Revenues (Expenses) section.

*Statements of Cash Flows* - Interest income earned on unspent bond proceeds would be reported as Investment Income, net of Investment Expenses under Cash Flows from Investing Activities.

- 3. Which transaction codes should have zero balance at fiscal year-end as a result of implementation of this Statement?**

The University would stop recording capitalized interest therefore, the following transaction codes for capitalized interest should have no balance at fiscal year-end 2020 and going forward.

<b>Transaction Code</b>	<b>DESCRIPTION</b>
TC 1302	Capitalized Investment Income - Other
TC 1303	Capitalized Investment Income - STIP
TC 1309	Capitalized Investment Income - SPWB Capital Leases
TC 2298	Contra Interest Expense-SPWB Cap Leases (payment of Cap. Interest)
TC 2299	Contra Interest Expense (payment of Cap. Interest)



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### 4. Which year-end closing steps would be eliminated as a result of implementation of this Statement?

The University would eliminate the following year-end closing steps related to capitalized interest starting fiscal year-end 2020.

FY19 Closing Step	DESCRIPTION
OP-19	Update and distribute UC Bond Funded Project Schedule to campuses.
23	Complete UC Bond Funded Projects schedule (BondProjectsXcampus-20YYcampus.xls) and submit to UCOP Capital Markets Finance. The data requested on the schedule is used to calculate interest income earned on tax exempt borrowed funds held at OP for projects under construction. This interest income is transferred to campuses to be recorded to the construction expenditure account as an offset to interest expense.
69	Provide interest income earned on borrowed funds held at OP for projects under construction to campuses to be recorded to the construction expenditure account as an offset to interest expense.
70	Record entries to construction expenditure accounts for interest income earned on borrowed funds held at OP for projects under construction.
OP-100	Provide interest rate to campuses to be used to calculate new year capitalized interest for projects funded by unrestricted funds.

### 5. How does implementation of this Statement impact annual asset file (CFSAST file)?

The University would stop using action code 7x to record capitalized interest for interest cost incurred before the end of a construction period effective July 1, 2019.