Asset Recognition - Council Policy

Effective Date	1 July 2010 (Ordinary Meeting of Council - 16 March 2011)
Policy Owner	Financial
Link to Corporate Plan	Strategic Theme 1: Effective and Inclusive Governance
Review Date	February 2013
Related Legislation	Nil
Related Documents	Authority in respect of this Policy is delegated to the Chief Executive Officer, Corporate Services General Manager, Chief Financial Officer, Financial Planning Co-ordinator

Policy Version	Approval Date	Adopted/Approved
1	15 April 2008	Ordinary Meeting of Council - 15 April 2008
2	16 March 2011	Ordinary Meeting of Council - 16 March 2011 (Effective 1 July 2010)

1. PURPOSE

To provide a framework for identifying, valuing and recording non-current physical and intangible assets. This policy aims to clarify the definition of and accounting recognition concepts for assets.

2. SCOPE

Nil

3. POLICY

3.1 Definition of an Asset

The Australian Infrastructure Financial Management Guidelines (the guidelines) define an asset as:

"A resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity".

The key features are that:

- The Council must control the asset;
- There was a past transaction or event which gave rise to the control; and
- There must be future economic benefits expected to flow to the agency.

Each of these features is discussed below.

<u>CONTROL</u>

The Council controls an asset if it has the power to obtain the future economic benefits flowing from the resource and to restrict the access of others to those benefits.

In determining the existence of an asset, the right of ownership is not essential. Council must simply have the ability to control the benefits which are expected to flow from the asset.

Council controls assets that they use in meeting their objectives.

Control is demonstrated by the ability of the Council to:

- use the asset to achieve its objectives;
- obtain a benefit from the sale of the asset;
- charge for the use of the asset; or
- deny use of the asset to other.

Other factors that must be considered in determining whether control exists are:

- access to the asset may be more relevant than mere possession or ownership; and
- ownership of an asset may not be necessary to control access to the benefits derived from the asset e.g. assets that are the subject of a finance lease.

<u>PAST TRANSACTION OR EVENT</u>

The assets of Council must result from past transactions or other past events. A contract to acquire an asset does not give rise to an asset, nor does the intent to acquire an asset. The asset must have been purchased, acquired or transferred to the control of Council prior to or at the date of the financial report.

<u>FUTURE ECONOMIC BENEFIT</u>

The future economic benefit embodied in an asset is the potential to contribute, directly or indirectly, to the flow of cash or cash equivalents to the Council. These benefits needs not necessarily be in the form of cash but can include revenue from a future sale, cost saving or other benefits resulting for the use of the asset by the Council.

In the case of Council, the future economic benefits may be in the form of providing goods and services in accordance with the Council's objects. The fact that Council does not charge, or does not fully charge, our customers for the goods and services it provides does not deprive those output of utility or value.

3.2 Asset Recognition Principles

Property, plant and equipment is defined in AASB 116 *Property, Plant and Equipment* as:

Intangible items that are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes and are expected to be used during more than one period.

In terms of AASB 116 and the guidelines, assets are only to be recognised by Council when:

- it is probable that future economic benefits will eventuate; and
- the asset possesses a cost or other value that can be measure reliably.

<u>PROBABILITY THAT FUTURE ECONOMIC BENEFITS WILL EVENTUATE</u>

In determining whether to recognise an asset, Council must consider the degree of uncertainty that attaches to the flow of future economic benefits from that particular asset. If it considers that it is more rather than less likely that future economic benefits will eventuate, then this section of the recognition test will be satisfied.

<u>RELIABLE MEASUREMENT</u>

The value of purchased goods and services can usually be measured reliably by the price charged by the supplier, while manufactured assets can be valued from labour and other costing inputs.

Where a cost cannot be measured reliably but it is probable that future economic benefits will eventuate, an asset is not be recognised. However, this must be disclosed in the notes to the financial statements.

3.3 Initial Recognition of Assets

Circumstances resulting in the initial recognition of assets include:

- acquisition involving consideration;
- assets acquired at no cost or for nominal consideration; and
- assets not previously recognised.

Recognition is the process of including the cost of the asset in the Council's asset register and in its financial statements.

The basis for measurement of the value of an asset is its cost of acquisition. In respect of an asset that is acquired at no cost, of for a nominal cost, the cost is its fair vale as at the date of acquisition.

Fair value is defined in AASB 116 as:

the amount for which an asset can be exchanged between knowledgeable, willing parties in an arm's length transaction.

For most infrastructure assets and public sector assets, a market type valuation is generally not available and its cost is measured at the carrying amount of the asset given up.

3.4 Capitalisation Vs Expensing of Costs Incurred

On initial recognition of an asset, or where subsequent costs are incurred, a decision must be made as to whether those costs are capitalised into the value of the asset or expensed through the Statement of Comprehensive Income.

On initial recognition, all costs incurred in purchasing or constructing the asset and getting it ready for use are capitalised to the value of the asset. Examples of these costs are provided below:

- its purchase price,
- any costs directly attributable to bringing the asset to the location and condition necessary to be capable of operating in the intended manner, and
- the initial estimate of the costs of dismantling and removing the asset and restoring the site, where the entity has this obligation.

Examples of directly attributable costs include:

- costs of employee benefits, directly related to the construction or acquisition of the asset,
- cost of site preparation;
- costs of initial delivery and handling;
- costs of installation and assembly;
- costs of testing less any process from sale of item produced directly attributable to the testing process and
- professional fees.

Not all costs are included as a cost of an asset. Examples of these costs are:

- costs of opening a new facility, and
- costs of introducing a new product or service (including costs of advertising and promotional activities).

3.5 Expenditure subsequent to Initial Purchase

MAJOR REPLACEMENTS

The cost of major replacements to non-current assets must be capitalised (refer AASB116 paragraph 13).

REPAIRS AND MAINTENANCE

Outlays that do not meet the criteria for recognition as an asset must be expensed as repairs and maintenance as incurred.

For example, expenditure that merely restores an asset to its original functionality, or repairs damage or wear and tear that would have prevented the asset reaching its original estimated useful life, must be expensed as repairs and maintenance.

REPLACEMENT OF COMPONENTS

For some complex assets, significant components with different estimated useful lives are separately identified for accounting purposes. Deciding whether expenditure on asset components should be capitalised follow the same process outlined for recognition, i.e. does the expenditure increase the annual service potential or useful life of the component beyond the originally assessed standard.

DAY-TO-DAY SERVICING

General day-to-day servicing of an item of property, plant and equipment is not to be capitalised into the cost of an asset. Generally, these costs will primarily be the costs of labour and consumables and may include the cost of immaterial parts. They are generally described as ‘repairs and maintenance’ and are recognised in the Statement of Comprehensive Income as incurred.

OVERHAULS/REFURBISHMENTS

Some items of property, plant and equipment may have parts which require replacement at regular intervals and in other instances, items may be renewed on an unplanned or ad hoc basis.

In these instances, Council will recognise the cost of such an item in the carrying amount of property, plant and equipment when that cost is incurred only if the asset recognition criteria are met. The carrying amount of those parts that are replaced will be derecognised.

PROVISIONS FOR FUTURE MAINTENANCE

The creation of a provision for future maintenance of non-current assets is not permitted as such action would be inconsistent with the principles for the recognition of provisions as detailed in AASB 137 *Provisions, Contingent Liabilities and Contingent Assets.* A provision is a liability and for a liability to be recognised, a past event must have occurred.

3.6 Classification of Assets

The classification of asset is one of the most important steps in financial reporting, asset accounting and asset management.

An asset class is a group of assets having a similar nature or function in the operations of Council, and which, for purposes of disclosure, is shown as a single item without supplementation disclosure. That is, a class is the lowest note level disclosure in the financial statements.

The asset class is the unit of reporting of assets in Council's financial statements. Assets of a similar nature and use in Council's operations are required to be grouped and disclosed as a separate class of asset in the financial statements.

COUNCIL'S ASSET CLASSES ARE:

- Land;
- Site improvements;
- Buildings;
- Plant and equipment;
- Furniture and fittings;
- Road and bridge network;
- Water infrastructure;
- Wastewater infrastructure;
- Stormwater;
- Gas Infrastructure;
- Heritage assets; and
- Intangible assets – computer software.
- Land Held for Resale

3.7 Asset Recognition Thresholds

Council usually controls a number of low value items that satisfy the asset recognition criteria, but if accounted for individually as assets would result in significant costs for limited benefits. To avoid such a situation and to facilitate a consistent threshold for reporting purposes, asset thresholds have been established.

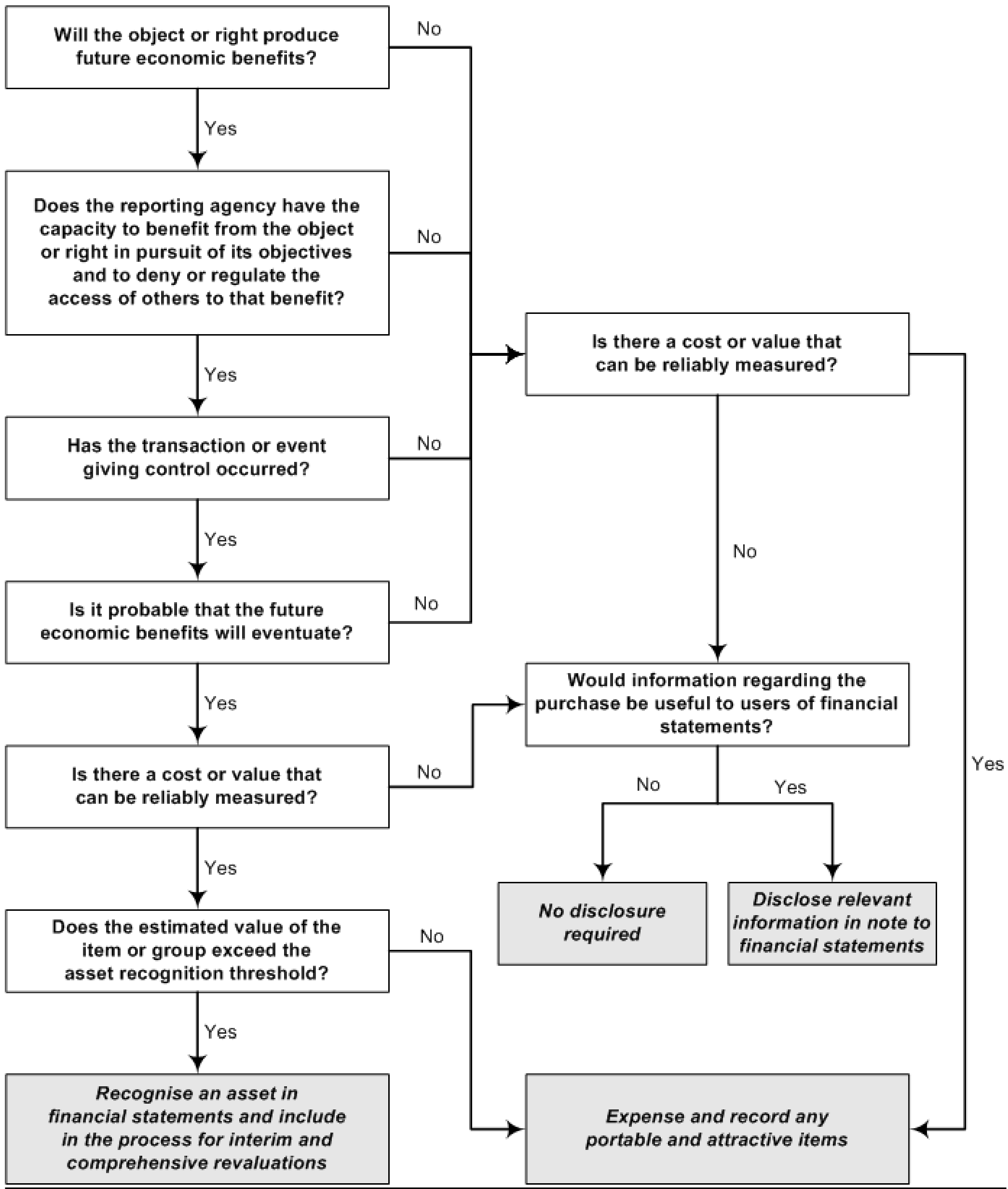
Section 154 of the Local Government (Finance, Plans and Reporting) Regulation 2010 requires the local government must, by resolution, set an amount for each different type of non-current physical asset below which the value of an asset of the same type must be treated as an expense.

	Asset Class	**Asset Recognition Threshold**	**Measurement Method**
Property, Plant and Equipment	Land	$1	Revaluation
	Land improvements	$5,000	Revaluation
	Buildings	$10,000	Revaluation
	Plant and equipment	$5,000	Cost
	Furniture and fittings	$10,000	Cost

	Asset Class	Asset Recognition Threshold	Measurement Method
Property, Plant and Equipment	Road and bridge network	$10,000	Revaluation
	Water infrastructure	$10,000	Revaluation
	Wastewater infrastructure	$10,000	Revaluation
	Stormwater	$10,000	Revaluation
	Gas Infrastructure	$10,000	Revaluation
	Heritage assets	$10,000	Revaluation
Intangibles	Computer Software	$10,000	Cost

Assets not recognised in previous periods that subsequently meet the recognition criteria shall be recognised from the date at the criteria are met.

3.8 Asset Recognition Flowchart



REVIEW TRIGGER:

- Periodic review