Accounting for Tangible Capital Assets

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Policy Statement

The adoption of a Tangible Capital Asset Policy is a prudent business practice that will strengthen corporate decision making through improved capital asset management and will provide increased reporting transparency to the Beaver Municipal Solutions/Beaver Regional Waste Management Services Commission (BMS/BRWMSC), the public and others.

The purpose of this policy is to establish consistent standards and guidelines for the planning, budgeting, and accounting for tangible capital assets. The Tangible Capital Assets Policy is required to:

- ensure "tangible capital assets" are recorded appropriately and accurately;
- provide for the amortization of tangible capital assets;
- ensure that all tangible capital asset acquisitions are planned for, acquired and financed in an appropriate and timely manner;
- ensure that all tangible capital asset disposals or write-downs are recorded in a timely manner;
- provide a framework for the annual capital budget review and approval process; and
- improve the management of the organization by promoting long term planning, prioritization and control of capital expenditures.

Definitions

<u>Amortization</u>
The reduction in the value of an asset due to usage, passage of time, wear and tear, technological outdating or obsolescence, depletion or other such factors. Sometimes known as depreciation, it is the method of attributing the historical or purchase cost of an asset across its useful life, roughly corresponding to normal wear and tear.

<u>Betterments</u>
Subsequent expenditures on tangible capital assets that enhance the service potential of the asset.

Service potential is enhanced by:
a) an increase in previously assessed physical output or service capacity;
b) lower associated operating costs; or
c) an improvement in the quality of the output.

Service potential enhancements may or may not increase in the remaining useful life of the tangible capital asset.

Capital Lease

A lease, with contractual terms, that transfers substantially all the benefits and risks inherent in ownership of property to the BRWMSC. For substantially all of the benefits and risks of ownership to be transferred, one or more of the following conditions must be met:

a) There is reasonable assurance that the BRWMSC will obtain ownership of the leased property by the end of the lease term.
b) The lease term is of such duration that the BRWMSC will receive substantially all of the economic benefits expected to be derived from the use of the leased property over its life span.
c) The lessor is assured of recovering the investment in the leased property and of earning a return on the investment as a result of the lease agreement.

Capitalization threshold

The value above which assets are capitalized and reported as non-financial assets in the financial statements.

Component

A part of an asset with a cost that is significant in relation to the total cost of that asset.

Cost

Purchased assets – cost includes the purchase price and other acquisition costs such as installation costs, design and engineering fees, legal fees, survey costs, site preparation costs, freight charges, transportation insurance costs, and duties.

Constructed or developed assets – cost includes the gross amount of consideration directly attributable to acquire control of, construct or develop the asset.

Donated or contributed assets – cost equals the fair value at the date of donation or contribution.

Fair value

The amount of consideration that would be agreed on in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

Market value

The estimated amount for which a property would be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction wherein the parties had each other acted knowledgeably, prudently and without compulsion. See also Fair Value.

Net book value

The cost of a tangible capital asset, less accumulated amortization and the amount of any write-downs.

Nominal value

The value assigned to an asset when no asset valuation method is relevant, or where the accuracy of any estimate could not be supported in an audit. Nominal value in this context is defined by the BRWMSC to be one Canadian dollar.

Residual value
The estimated net realizable value of a tangible capital asset at the end of its useful life.

Service potential
The tangible capital asset's output or service capacity, normally determined by reference to attributes such as physical output capacity, quality of output, associated operating costs and useful life.

Tangible capital assets
Non-financial assets having physical substance that:
a) are held for use in the production or supply of goods and services, for rental to others, for administrative purposes or for the development, construction, maintenance or repair of other tangible capital assets;
b) have useful economic lives extending beyond an accounting period;
c) are to be used on a continuing basis; and
d) are not for sale in the ordinary course of operations.

Useful life
The estimate of either the period over which the BRWMSC expects to use a tangible capital asset or the number of production or similar units that it can obtain from the tangible capital asset. The life of a tangible capital asset may extend beyond its useful life. The life of a tangible capital asset, other than land, is finite, and is normally the shortest of the physical, technological, commercial and legal life.

Write-down
The reduction in the cost of a tangible capital asset to reflect the decrease in the quality or quantity of its service potential due to a permanent impairment, and the BRWMSC still owns the asset written down. A write-down should not be confused with a "write off", which is treated as a disposal.

Guidelines

1. Asset Definitions & Classification

   1.1. Capitalization

   Tangible capital assets that have an acquisition value per individual item or unit that exceeds the following capitalization thresholds by asset type will be capitalized:

   a) All Land $0
   b) Land Improvements $ 2500
   c) Buildings $ 2500
   d) Engineered Structures $ 2500
   e) Machinery & Equipment $ 2500
   f) Vehicles $ 2500

The following assets will not be capitalized:

- land (or other assets) acquired by right, such as Crown lands, forests, water and mineral resources;
- works of art and historical treasures; and
- intangible assets such as patents, copyrights and trademarks.

1.2. Classification

Tangible capital assets will be classified in the following major categories:

- Land
- Land Improvements
- Buildings
- Engineered Structures
- Machinery & Equipment
- Vehicles

1.3. Capital Leases

The BRWMSC will account for a capital lease as an acquisition of a tangible capital asset and incurrence of a liability. The cost of a leased tangible capital asset is determined in accordance with Public Sector Guidelines PSG-2, Leased Tangible Capital Assets.

2. Recording Assets

2.1. When to Record Tangible Capital Assets

A physical asset will be recorded as a tangible capital asset in the BRWMSC financial statements as of the date it meets the definition of a tangible capital asset. Control of the asset's economic benefit is a key concept in determining if and when to record a tangible capital asset for the BRWMSC. The BRWMSC does not have to legally own an asset to have control and management responsibility of that asset.

2.2. Betterments vs Maintenance

Betterments which exceed the capitalization threshold of the applicable capital asset class will be included in the tangible capital asset's cost. Any other expenditure would be considered a repair or maintenance and expensed in the period.

2.3. Single asset versus asset division into components and/or segments

Tangible capital assets may be accounted as a single asset or by components. A linear asset (i.e. roads or transmission lines, utility service networks) may also be accounted for by segments or a combination of segments and components. Whether the component and/or segment approach is to be used will be determined by the usefulness of the information versus the cost of collecting and maintaining information at the more detailed component or segment level.

2.4. Grouped/Pooled Assets

Assets that have an individual unit value less than the corresponding capitalization threshold (on their own) but have a material value as a group can be 'grouped' as a single asset with one combined value in the asset accounting records.

3. Asset Valuation

3.1. Definition of Cost

Tangible capital assets should be recorded at cost plus all ancillary charges necessary to place, prepare, and install the asset in its intended location and condition for use. Cost includes all non-refundable taxes and is net of any trade discounts or rebates.

Capital grants or donations towards a purchase or construction or betterment of a tangible capital asset are not netted against the cost of the related tangible asset.

3.2. Donated or Contributed Assets

For donated or contributed assets that meet the criteria for recognition as tangible capital assets, cost is equal to the fair value at the date of donation or contribution. Fair value may be determined using market or appraisal values. If it is not practical to determine the fair market or appraised value, use a reasonable estimated cost. Ancillary costs necessary to place, prepare, and install the donated asset in its intended location and condition for use should be capitalized.

4. Amortization Methods & Estimated Useful Life

4.1. Amortization

The cost, less any residual value, of a tangible capital asset with a limited life should be amortized over its useful life in a rational and systematic manner appropriate to its nature and use. Land has an unlimited useful life and should not be amortized. No amortization should be recorded on tangible capital assets which have been removed from service but not yet physically disposed of either through sale, demolition/dismantling, trade-in or transfer.

4.2. Estimated Useful Life

An asset's useful life is based on the BRWMSC's planned use of that asset and experience with other similar assets.

4.3. Residual Values

In most cases, the BRWMSC will hold a tangible capital asset for an extended period of time and as a result, the residual/salvage value will be immaterial for most asset classes. A residual value may be recorded for a tangible capital asset when the responsible department believes that the asset will have a significant value beyond its useful life to the BRWMSC.

5. Review and Write-downs

5.1. Revising Amortization Methods and Estimated Useful Life

The amortization method and the estimated remaining useful life should be reviewed on a regular basis by the responsible department with assistance from accounting, and revised when the appropriateness of a change can be clearly demonstrated.

The effect of a change in the estimated useful life of a tangible capital asset and its associated effect on amortization expense are allocated to the period of revision and applicable future periods.

5.2. Write-down for Impairment

A write-down for impairment of a tangible capital asset is required when either:

- service potential is impaired (ie. the asset no longer contributes to the BRWMSC's ability to deliver goods or services); or
- future economic benefits are impaired (ie. the net book value of the tangible capital asset is in excess of the future economic benefits expected from its use and this excess is expected to be permanent).

  Write-downs of tangible capital assets should be recorded as a current period expense in the period that the decrease can be measured and is expected to be permanent. Both conditions are required to write down the asset. Write-downs are permanent and cannot be reversed in subsequent periods even if circumstances change.

6. Maintaining Records

The CFO will maintain a record of the related asset description, details of the asset, and the date in use when tangible capital assets are purchased, acquired, developed, improved, constructed, or donated. Accounting is responsible for ensuring the accounting records are adjusted based on the information provided by the responsible department.

The CFO will periodically review the accounting records to ensure that they are current, accurate, and complete. The CFO is responsible to ensure that periodic asset inventories are performed and documented.

7. Asset Disposal

When tangible capital assets are taken out of service, destroyed, replaced due to obsolescence, scrapped, abandoned, dismantled or otherwise written off, the responsible department will notify the CFO and accounting of the related asset description, details of the asset disposal (i.e. proceeds on sale or transfer or trade-in), and the effective date of the change in the use of the asset. Any gain or loss on the disposal will be recorded as a revenue or expense, respectively, in the period of the disposal.

The CFO will establish procedures for the method of disposal of uneconomic assets, including public tendering of asset sales, and procedures regarding negotiations to sell land holdings.

Results will be reported to the Board.

Any asset acquired through a government grant and sold in the future will require Municipal Affairs approval.

8. Financial Reporting & Budgeting

8.1. Amortization

Amortization is accounted for as an expense in the statement of operations.

8.2. Disclosure Required

In total and for each major category of capital assets, the BRWMSC will disclose the following in the annual financial statements:

a. Cost at the beginning and end of the period;
b. Additions in the period;
c. Disposals in the period;
d. The amount of any write-downs in the period;
e. The amount of amortization for the period;
f. Accumulated amortization at the beginning and end of the period;
g. Net carrying amount at the beginning and end of the period.

8.3 Budgeting and Approvals

Expenditures for tangible capital assets will be included in the BRWMSC's budget process and approved by the Board.

Emergent capital projects and awarded capital project expenditures that are projected to go over their approved budget, including contingency allowances, must be reviewed and approved in advance:

a) For amounts totalling $50,000 or less – by the GM.
b) For amounts greater than $50,000 – by the Board.

A recommendation to change the funding, or substantially change the scope or expected outcome of an approved capital project (with or without a financial impact) must be reviewed and approved in advance by the Board.

In all cases, a business case must be completed and the source of the additional funds required must be identified.

Roles and Responsibilities, Procedures, Forms and Related Policies

1. The Vice President Corporate Services and Chief Financial Officer (CFO) will administer this Policy through the General Manager.

2. Attachments: N/A

3. Related Policies:

   a) FIN-005 Debt Management