COUNCIL
APPROVED
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GOEDGEKEUR
RAAD

B64/4
Ndanduleni Makhari (012 358 8100/1)
COUNCIL: 29 May 2008

11. FINANCIAL SERVICES DEPARTMENT (ASSET AND DISPOSAL MANAGEMENT DIVISION)
PROPOSED REVISIONS TO THE POLICY FOR THE CORPORATE MANAGEMENT OF THE PROPERTY, PLANT AND EQUIPMENT REGISTERS
(From the Portfolio Committee: Finance: 10 April 2008)

1. PURPOSE

The aim of the report is to obtain approval of the proposed revisions to the Policy on the corporate management of the Property, Plant and Equipment Registers so as to establish guidelines for the management and control of assets acquired by the municipality that must be recognised in the relevant registers.

2. STRATEGIC OBJECTIVE

SO5: To ensure good governance, financial viability and optimal transformation capacity to execute its mandate.

3. BACKGROUND

Subsequent to the Auditor-General's report for the 2005/06 financial year of the CoT, various shortcomings in the interpretation and application of accounting standards to the assets on the Property, Plant and Equipment Registers were identified.

Due to inadequate capacity within the municipality the services of external service providers were obtained to assist in addressing the shortcomings mentioned above.

The need for a standards compliant register was highlighted in the report of the Auditor-General. In order to ensure that the necessary procedures and processes are implemented the requisite approvals for the various management principles as derived from the accounting standards are requested.

4. THE STATUS QUO

The approved assets management policy makes provision for the following:

- Threshold value
- Procedures
  - Capitalisation
  - Acquisitions
  - Capital projects and
  - Management of the register.

An extensive handling of the above topics are contained in the policy which was approved on 2006-02-17.

5. PROPOSED REVISIONS

A review of the above mentioned policy was done and it was found to be inadequate in that it did not address the following topics which are standards that have been prescribed by the Accounting Standards Board, National Treasury and legislation:

- Threshold value
- Intangible Assets
- Agricultural Assets
- Heritage Assets
- Rehabilitation Costs
- Component Accounting
- Useful Life
- Environmental Assets
- Investment Property
- Impairment
- Inventories
- Leases
- Construction Contracts
- Non-Current Assets held for sale
- Responsibility for Asset Management
- Subsequent Expenditure on Assets

An extensive treatment of each of the above topics is attached to this report.

6. IMPLICATIONS

6.1 Financial

Not applicable

6.2 Human Resources

Compliance and implementation of the proposed Management Principles above is dependent on approval of the revised Policy by the Council. In order to implement the principles, systems will have to be updated to reflect the new revised principles. Impact on the financial statements, the accounting policy, budgetary process and systematic processes is anticipated and all relevant stakeholders must be taken on board. It is therefore suggested that the following factors be considered prior to the approval of the principles:

1) The documents submitted are merely proposals that need to be scrutinized to see whether they can indeed be implemented, whether there are any obstacles for implementation, concerns or other issues (whether from a financial, budgetary or any other perspective) that might jeopardize the successful and full execution of the principles.

2) Once there is agreement from all stakeholders on all the principles then the final documents can be submitted to the Steering Committee for approval.

3) Business processes, procedures etc. must then be developed on interpretation of the approved principles.

4) Once this has been done then the principles can be congregated into a compact, summary policy for the management of PPE which can then be submitted for approval by the Council.

In order to expedite the implementation and compliance process it is therefore suggested that a robust, compact and urgent consultation exercise be arranged for all the Business Area Managers. The aim of the consultation is to ensure timely compliance to the prescribed standards by the municipality. It needs to be mentioned that it is anticipated that the next round for the auditing of the Property, Plant and Equipment Registers will commence in May 2008.

6.3 Communication

Not applicable

6.4 Legal

Not applicable

7. COMMENTS OF THE EXECUTIVE DIRECTOR: LEGAL SERVICES

(Unaltered)

The report on the policy statements for the corporate management of CoT property, plant and equipment register goes a long way in addressing any possible concerns of the AG and is therefore supported.

8. COMMENTS OF THE CHIEF FINANCIAL OFFICER

(Unaltered)

I agree with the recommended procedures as set out in the report. The policies as attached to the report, must ensure that the requirements of the accounting standards are met, and that the issues as raised by the Auditor-General in his report of 2006/07 is addressed.

9. CONCLUSION

In order to achieve a fully GAMAP/GRAP Compliant accounting process for the assets of the CoT, it is imperative that an Asset Management Policy is developed. With the development of the management proposals in this report, which will guide the revision of the existing policy, a way has been chartered to reach such an outcome.

ANNEXURE:

A: Various Policy statements for the Corporate Management of the Property, Plant and Equipment register

RESOLVED:

1. That the Policy Statements on the Corporate Management of the Property, Plant and Equipment attached to the report be approved.

2. That an expeditious consultation process dealing with the proposed revised management principles with all Senior Managers of the CoT be arranged and presented.

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ASSET MANAGEMENT POLICY

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ACCOUNTING POLICIES

3. Detailed policies and procedures

3.1 Property, plant and equipment

3.1.1 Introduction

1. This policy does not apply to:

- *Biological assets related to agricultural activity (Refer to CoT's policy on Agriculture);*
- *Recognising and measuring exploration and evaluation assets;*
- *Mineral rights and mineral reserves such as oil, natural gas and similar non-regenerative resources;*
- *Property, plant and equipment classified as held for sale in accordance with 'Non-current assets held-for-sale and discontinued operations' (Refer to CoT's policy on Non-current assets held-for-sale and discontinued operations); and*
- *Investment properties that have been completed or to investment properties that are being redeveloped for continued future use as investment properties. (Refer to CoT's policy on Investment properties)*

2. A property that is being constructed or developed for future use as an investment property is subject to the rules in this policy until such time as it is complete, from which point the rules under investment property then applies. (Refer to CoT's policy on Investment properties)

3.1.2 General

3. *Property, plant and equipment is defined as* tangible 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.*

4. Assets are defined as resources controlled by the CoT as a result of past events and from which future economic benefits are expected to flow to the entity.

5. Tangible assets are those assets that have physical substance. Assets that do not have physical substance must be accounted for in terms of CoT's policy on intangible assets.

6. Items of property, plant and equipment are recorded initially at cost.

Useful life and depreciation

7. A tangible fixed asset has a useful life, after which it is no longer of use to the CoT. The useful life of an asset includes any period after acquisition when the asset is capable of operating in the manner intended by management, but has not yet been brought into use. Refer to CoT's policy on useful life.

8. *The depreciable amount of an asset is the cost of an asset or other amount substituted for cost, less its residual value.*

   - *Other amount may refer to the fair value of the asset, where the CoT has a policy of revaluation.*
   - *Residual value is addressed in the CoT's policy on residual values.*

9. *Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life.*

Impairments

10. *Impairments are the amount by which the carrying amount of an asset exceeds its recoverable amount. Please refer to CoT's policy on impairments.*

11. *The carrying amount of an item of property, plant and equipment is the amount at which the asset is recognised after deducting any accumulated depreciation and accumulated impairment losses.*

3.1.3 Recognition of initial costs

12. *The cost of an item of property, plant and equipment should be recognised as an asset when:*

    - *it is probable that future economic benefits associated with the item will flow to the entity; and*
    - *the cost of the item can be measured reliably.*

13. *Cost is defined as the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition or construction or, where applicable, the amount attributed to that asset when initially recognised. Other consideration could, for example, include an asset given up in exchange.*

14. *Sufficient certainty that future economic benefits will flow to the CoT is normally achieved only when the risks and rewards of the asset have passed to it. Before this, the transaction can usually be cancelled without significant penalty and, therefore, the asset is not recognised. Normally, the transfer of risks and rewards is assumed to occur when an unconditional and irrevocable contract is put in place. Where there is a commitment, but no binding contract, such commitments are disclosed, but the asset is not recognised.*

15. *Generally, it is clear in establishing whether an item should be recognised as property, plant and equipment. In the case of disputes, the Chief Financial Officer shall be responsible for the final recognition of an item as property, plant and equipment*

Disaggregation ("Component accounting")

16. *Disaggregation ("Component accounting") is the separation of an asset into its significant components. This is necessary because this policy requires that each part of an item of property, plant and equipment that has a cost that is significant in relation to the total cost of the item, must be depreciated separately.*

17. *Please refer to CoT's policy on "component accounting"*

Aggregation of items of property, plant and equipment

18. *This policy allows for individual items to be aggregated and treated as a single item of property, plant and equipment.*

19. *This implies that the recognition criteria must be applied to the aggregate value of the items of property, plant and equipment.*

20. *These items of property, plant and equipment will be recognised as a separate class of property, plant and equipment.*

21. *The aggregation of items of property, plant and equipment as a single item must be approved by the Chief Financial Officer.*

Spare parts

22. *Major spare parts and stand-by equipment should be treated as property, plant and equipment when they are expected to be used during more than one period. In the same way, if the spare parts or servicing equipment can only be used in connection with an item of property, plant and equipment they are accounted for as property, plant and equipment.*

23. *Where this is the case, the spare parts or servicing equipment would be depreciated over a period that does not exceed the useful life of the related asset.*

Environmental assets

24. *Due consideration must be given to situation's where items of property, plant and equipment are acquired that, by themselves, may not generate economic benefits, but which are necessary to enable other assets to do so.*

25. *Examples are assets necessary to ensure safety or to comply with environmental regulations. Such assets should be recognised because they enable other assets to generate economic benefits in excess of the benefits that could otherwise have been derived from those assets.*

26. *Please refer to Cot's policy on environmental assets.*

3.1.4 Recognition of subsequent costs

3.1.4.1 General

27. *Once an item of property, plant and equipment is recognised and capitalised, the CoT may incur further costs on that asset at a later date.*

28. *An assessment of all subsequent expenditure must be made to determine whether this should be capitalised or expensed.*

29. *Please refer to CoT's policy on subsequent expenditure.*

3.1.4.2 Significant components (Component accounting)

30. *When a component is replaced or restored, the old component is written off, to avoid double counting and the new component capitalised, if its cost is recoverable.*

31. *The costs of a replacement component must be recognised as an asset if they meet the recognition criteria above.*

32. *If such costs meet those criteria and are capitalised the carrying amount of the part or parts that are replaced is derecognised, that is the accumulated cost and depreciation of the replaced parts is eliminated.*

33. *This applies whether or not the replaced part or component had been separately depreciated. If the cost and depreciation of the replaced part or component cannot be identified it is acceptable to use the cost of the replacement as a proxy for the cost of the replaced part when it was acquired or constructed.*

34. *Where components of an asset have been separately identified, the components need not be disclosed separately in the fixed asset table in the notes to the financial statements, as they do not constitute separate classes of assets.*

3.1.4.3 Major inspections or overhauls

35. *A condition of continuing to operate an item of property, plant and equipment may be performing regular major inspections for faults regardless of whether parts of the item are replaced.*

36. *As noted in the CoT's policy on subsequent expenditure, the costs of day-to-day servicing of an item do not meet the asset recognition criteria. However, major repair and maintenance programmes carried out as part of a periodic inspection and overhaul and that result in future economic benefits may well qualify for recognition.*

37. *The recognition of major inspection costs is dependant on whether or not repair and maintenance costs meet the criteria for recognition as an asset.*

38. *When each major inspection is carried out the cost is recognised as part of the carrying amount of the item of property, plant and equipment as a replacement if it meets the asset recognition criteria in the standard.*

39. *Any remaining carrying amount relating to the previous inspection must be derecognised.*

40. *This treatment applies regardless of whether or not the cost of the previous inspection was separately identified and depreciated when the item was acquired or constructed.*

41. *Where the cost of the previous inspection was not separately identified the estimated cost of a future similar inspection may be used as a proxy for the cost of the previous inspection when calculating the carrying value of the previous inspection that needs to be derecognised.*

42. *The actual cost of the overhaul or inspection is then capitalised, provided that it meets the recognition criteria, that is, it is probable that future economic benefits will flow to the entity and the cost can be measured reliably.*

43. *This inspection/overhaul cost must be depreciated over the period to the next inspection/overhaul.*

44. *The cost and depreciation attributed to the overhaul originally must be removed from the balance sheet once the cost of the new overhaul has been capitalised to avoid double counting.*

45. *The remainder of the asset will be depreciated over the full useful life of the asset, on the basis that the appropriate overhauls will be carried out as they are due.*

46. *The same approach applies even if the cost of overhaul/inspection was not separately identified and depreciated. This should not often occur in view of the requirement to adopt this treatment for significant parts or components.*

47. *Losses arising on derecognition of the carrying amount of the previous inspection costs represents the under-depreciation in the past of the inspection/overhaul element.*

48. *The recognition and derecognition of major inspection costs must be approved by the Chief Financial Officer.*

3.1.5 Initial measurement of property, plant and equipment

3.1.5.1 General

49. *Items of property, plant and equipment that qualify for recognition must be initially measured at cost.*

50. *Measurement of cost is generally the price paid.*

51. *Where an asset is self-constructed, the production cost will be ascertained by aggregating the price paid for material, labour and other inputs used in the construction.*

52. *The cost of an item of property, plant and equipment comprises:*

- *The purchase price, including import duties and non-refundable purchase taxes less any trade discounts and rebates.*
- *Directly attributable costs of bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.*
- *The initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located. The obligation to incur these costs arises either when the item is acquired or as a result of using the item during a particular period other than for the purpose of producing inventories during that period. (Refer CoT's policy on rehabilitation costs)*

53. *This is the case even if assets were acquired at a bargain and, therefore, the purchase cost does not reflect the full value of the asset.*

54. *Examples of directly attributable costs are:*

- *The cost of employee benefits as defined in 'Employee benefits' that arise directly from the construction or acquisition of the item.*
- *The costs of site preparation.*
- *Initial delivery and handling costs.*
- *Installation and assembly costs.*
- *Professional fees.*
- *Costs of testing whether the asset is working properly (commissioning costs), after deducting the net proceeds of sale of any 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 such as samples produced during testing).*

55. *Employee benefits are defined as all forms of consideration given by the CoT in exchange for services rendered by employees. The types of benefit include:*

- *Short-term employee benefits such as wages, salaries and social security contributions, paid annual leave and paid sick leave, profit sharing and annual bonuses and non-monetary benefits such as medical care, cars, housing and free or subsidised goods or services.*
- *Post-employment benefits such as pensions, other retirement benefits, post-employment life insurance and post-employment medical care.*
- *Other long-term employment benefits, including long service leave or sabbatical leave, jubilee or other long-service benefits, long-term disability benefit and deferred bonuses or profit sharing and other deferred compensation.*
- *Termination benefits.*

56. *Not all of the above costs will be eligible or relevant even then. For example, termination benefits paid to employees who have left employment would not be relevant as they would not be involved in constructing the asset.*

57. *Only the costs that are directly attributable to the item of property, plant and equipment, and not the general operating costs, may be capitalised.*

58. *The following are types of costs that are not directly attributable:*

- *Costs of opening a new facility.*
- *Costs of introducing a new product or service (including costs of advertising and promotional activities).*
- *Costs of conducting business in a new location or with a new class of customer (including costs of staff training).*
- *Administration and other general overhead costs.*

59. *Costs may be capitalised until the asset is "capable of operating in the manner intended by management".*

60. *Where an asset is purchased or constructed and can operate in that manner immediately, but is not brought into use immediately, costs incurred whilst the asset is standing idle may not be capitalised.*

61. *Costs incurred in using or redeploying an item is not included in its carrying amount. Examples of such costs are:*

- *Costs incurred while an item that is capable of operating in the manner intended by management has yet to be brought into use or is operated at less than full capacity.*
- *Initial operating losses, such as may be incurred while demand for an item's output builds up.*
- *Costs of relocating or reorganising part or all of an entity's operations.*

3.1.5.2 Start-up costs

62. *Start-up costs and similar pre-production costs do not form part of the cost of an asset.*

63. *Initial operating losses incurred prior to an asset achieving its planned performance must be recognised as an expense. The same would apply to operating losses that occur because a revenue earning activity was suspended during the construction of a tangible fixed asset.*

64. *In relation to start-up costs a distinction must be drawn between a commissioning period for plant, where the plant cannot yet physically operate at normal levels, and a start-up period where plant can operate at normal levels, but it is not doing so because demand has not yet built up.*

65. *The costs of an essential commissioning period must be capitalised. Where the asset is ready for use, but demand has not yet built up, such costs must be expensed.*

3.1.5.3 Rehabilitation costs

66. *Rehabilitation costs refer to the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located. The obligation to incur these costs arises either when the item is acquired or as a result of using the item during a particular period other than for the purpose of producing inventories during that period.*

67. *Please refer to the CoT's policy on rehabilitation costs for further details.*

3.1.5.4 Self-constructed assets

68. *The cost of a self-constructed asset is determined using the same principles as for an acquired asset.*

69. *Capitalisation of general and administrative overheads and start-up costs are prohibited.*

70. *One exception to this rule, however, might be self constructed assets that are of a kind that the CoT may produce for sale, the cost of which is, therefore, determined in accordance with the inventory rules. The cost of inventories includes costs of conversion. Costs of conversion include a systematic allocation of fixed and variable production overheads. Fixed production overheads are indirect costs of production and include depreciation and maintenance of factory buildings and equipment and the cost of factory management and administration. In the above special case a proportion of overheads relating to general management and administration would be included in cost.*

71. *The above rule can only be applied on the authorisation of the Chief Financial Officer.*

72. *The cost of abnormal amounts of wasted material, labour or other resources incurred in the production of a self-constructed asset are not included in the cost of the asset.*

3.1.5.5 Labour costs

73. *Only those directly attributable labour costs (employee benefits) that relate to the time spent by employees on constructing or acquiring the specific asset should be capitalised.*

74. *Time spent on other potential acquisitions or developments cannot be included.*

75. *For example, an internal surveyor may carry out surveys on five different properties as part of the process to determine which one of those properties the company will buy. However, only the surveyor's time in respect of the survey on the successful property should be capitalised as part of the asset.*

76. *Furthermore, if a site engineer spends 30 per cent of his time on a particular development project, then only 30 per cent of his employee costs must be capitalised as part of the asset's cost.*

77. *Other overhead costs should not be capitalised, unless the asset is of a type that the CoT also produces for sale and the overheads would qualify for inclusion in cost.*

78. *Where the asset is not of a type that is produced by the CoT for sale, it is not permitted to capitalise the general overheads.*

79. *As a general rule only incremental costs that would have been avoided had an asset not been constructed can really be directly and conclusively attributed to bringing the asset to its working condition and therefore capitalised to the asset.*

80. *For example, the cost of a temporary office on the site of the development, that would not have been incurred but for the project, should be capitalised because it is both an incremental and a direct cost that is attributable to bringing the asset to the condition necessary for it to operate in the manner intended by management.*

3.1.5.6 Professional fees

81. *External professional fees incurred in finding a suitable asset, which is then acquired or constructed, may be capitalised.*

82. *Costs such as external professional fees should only be capitalised as part of the cost of an asset when they relate directly to the acquisition or construction of the asset.*

83. *Costs on speculative projects and costs of aborted plans should not be capitalised.*

84. *Other professional fees incurred in acquiring an asset such as legal fees and stamp duty must be included in the cost of an asset.*

85. *The labour costs of the CoT's own employees searching for suitable sites or assets cannot be included within the costs to be capitalised.*

3.1.5.7 Other incremental costs

86. *Although constructing or acquiring a new asset may result in other incremental costs that would have been avoided only if the asset had not been constructed or acquired, these should not be included in the cost of the asset if they do not bring the asset into the location and condition necessary for it to be capable of operating in the manner intended by management.*

87. *Costs that do not relate to the construction of the physical asset, but rather relate to setting up the new business as a whole do not qualify to be capitalised as part of the cost of the asset.*

88. *Examples of such costs are as follows:*

- *market research;*
- *accounts staff;*
- *advertising;*
- *Training costs; and*
- *head office costs during the construction phase.*

3.1.5.8 Software development costs

89. *Computer software development costs may arise in several ways. In some cases an asset comprises both tangible and intangible elements and judgement is needed to determine which element is more significant.*

90. *For example, computer software for a machine that cannot operate without that specific software is an integral part of the machine and is treated as property, plant and equipment.*

91. *The same applies to an operating system of a computer. Where software is not an integral part of the related hardware, it is treated as an intangible asset.*

92. *With respect to intangible assets, refer to CoT's policy on this matter.*

3.1.5.9 Period of capitalisation of directly attributable costs

93. *Capitalisation of costs can only take place in respect of the period in which the activities necessary to bring the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.*

94. *Capitalisation should cease when substantially all the activities necessary to get the asset ready for use are complete, even if the asset has not yet been brought into use.*

95. *'Ready for use' means when the physical construction of the asset is complete even though routine administrative work might still continue.*

96. *For example, if minor decoration of a property to a purchaser's specification is all that is outstanding this indicates that the asset is substantially complete.*

97. *Heads of departments must define the stage and criteria that must be met for a capital project/acquisition to be classified as ready for use. Heads of departments must inform the chief financial officer once an asset is ready for use as the asset will have to be capitalised at that date into the fixed asset register.*

98. *All capital projects and acquisitions must be reviewed on an annual basis to determine if they meet the criteria "ready for use" and therefore must be capitalised.*

99. *The timing for the review would be provided by the chief financial officer in terms of the terms of CoT's asset management procedures.*

3.1.6 Leases

100. Assets leased under a finance lease are recorded in accordance with the CoT's policy on leases.

3.1.7 Government grants

101. The carrying amount of assets may be reduced by the amount of government grants.

102. Government grants must be accounted for in terms of CoT's policy on government grants

3.1.8 Exchanges of assets

103. An item of property, plant and equipment may be acquired in exchange for another non-monetary asset or for a combination of non-monetary and monetary assets. The cost of such an acquired item is measured at fair value unless:

- *the exchange transaction has no commercial substance; or*
- *the fair value of neither the asset received nor the asset given up can be reliably measured.*

104. This applies even if the CoT cannot immediately derecognise the asset given up.

105. Fair value is defined as the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.

106. If the acquired item is not measured at fair value it is measured at the carrying amount of the asset given up.

107. Carrying amount is defined as the amount at which an asset is recognised after deducting any accumulated depreciation and accumulated impairment losses.

108. Where the consideration received comprises a combination of non-monetary and monetary assets the fair value is adjusted by the amount of the monetary assets (for example, cash) given or received.

109. For example, the CoT exchanges surplus land with a book value of R 100 000 for cash of R 200 000 and plant and machinery valued at R 250 000. The transaction has commercial substance. The plant and machinery is recorded at R250 000, which is equivalent to the fair value of the land of R 450 000 less the cash received of R 200 000.

110. A transaction has commercial substance if the difference in either of the two bullet points below is significant relative to the fair value of the assets exchanged:

- *The configuration of the cash flows of the asset received differs from the configuration of the cash flows of the asset given up.*
  - *Configuration of the cash flows means the risk, timing and amount of the cash flows.*
- *The entity-specific value of the part of the entity's operations affected by the transaction changes as a result of the exchange.*
  - *Entity-specific value is defined as the present value of the cash flows an entity expects to arise from the continuing use of an asset and from its disposal at the end of its useful life or expects to incur when settling a liability.*

111. *Where there are no comparable market transactions the fair value of either the asset given up or the asset received can still be reliably measured if:*

- *the range of reasonable estimates of fair value does not vary significantly, that is if the range is reasonably narrow; or*
- *if the range itself is not narrow, the probabilities of the various estimates within the range can be reasonably assessed and used in estimating fair values.*

112. *Where both the fair value of the asset given up and the fair value of the asset received can be estimated with equal reliability, the fair value of the asset given up is used to measure the cost of the asset received.*

113. *However, if the fair value of the asset received can be measured with more reliability, then that value is used.*

114. *Exchanges should have commercial substance and be capable of reliable measurement before fair value may be used and gains recognised, will often result in the same accounting treatment for exchanges of similar assets as in the past.*

115. *It is important to note that for an exchange transaction to be measured at fair value the transaction must have both of the characteristics, that is commercial substance and reliability of measurement.*

116. *A transaction that has no commercial substance, but can be reliably measured should be recorded at the carrying amount of the asset given up. In such a transaction the fair value of the item received may give evidence of impairment in the carrying amount of the item given up.*

117. *Exchange of assets can only occur on the approval of council. The chief financial officer will, in accordance with the above policy, determine the costs of the asset.*

3.1.9 Measurement subsequent to initial recognition – The cost model

118. *Subsequent to initial recognition the CoT applies the cost model as its accounting policy.*

119. *This model is applied to the whole of a class of property, plant and equipment and not merely to individual assets within a class.*

120. *The cost model requires that, after initial recognition, property, plant and equipment should be carried at cost less accumulated depreciation and accumulated impairment losses.*

3.1.9.1 Class of assets

121. *The CoT has the following classes of assets:*

- *Land;*
- *Land and buildings;*
- *Electricity;*
- *Roads and stormwater;*
- *Water and sanitation;*
- *Plant;*
- *Machinery;*
- *Aircraft;*
- *Motor vehicles;*
- *Furniture and fittings; and*
- *Office equipment.*

122. *The chief financial officer can on an annual basis update the class of assets when the need arises.*

3.1.10 Measurement subsequent to initial recognition - The revaluation model

3.1.10.1 General matters

123. *Currently, the CoT does not apply the revaluation model for its property, plant and equipment.*

124. *The use of the revaluation model can only be applied on the recommendation of both the chief financial officer and municipal manager and approval of council. The section on revaluations becomes applicable only approval of council.*

125. *The revaluation model requires that, subsequent to initial recognition, property, plant and equipment whose fair value can be reliably measured should be carried at a revalued amount, being fair value at the date of revaluation, less any subsequent accumulated depreciation and any subsequent accumulated impairment losses.*

126. *Revaluations must be carried out with sufficient regularity that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date.*

127. In applying the for approval of the revaluation policy, the following factors must be clearly addressed in the updated policy document:

- *The items of property, plant and equipment that are to be revalued;*
- *The timing of revaluations; and*
- *The valuation basis to be used.*

128. Once council approves a policy of revaluation, this policy must be applied to all assets within an individual class of assets and the valuations must be kept up-to-date at current fair values.

129. If a single item of property, plant and equipment is revalued, then the entire class of property, plant and equipment to which that item belongs should be revalued, although the policy need not be applied to all classes of property, plant and equipment.

3.1.10.2 Frequency of revaluations

130. One of the requirements is that valuations should remain up-to-date, as old valuations that do not reflect current values are meaningless.

131. The chief financial officer must in terms of the asset management procedures determine the frequency of revaluations. This must be based on the following factors:

- *The movement in the fair value of property, plant and equipment.*
- *The volatility of the fair value.*
- *Changes in the general market conditions;*
- *The condition and location of the asset*

132. The Chief Financial Officer must maintain a process by which the CoT can monitor the movements in fair value each year, even if this does not amount to a full annual revaluation.

3.1.10.3 Valuers

133. Valuation of land and buildings should be undertaken by professionally qualified valuers.

134. A qualified valuer should be a person who:

- *Holds a recognised and relevant professional qualification.*
- *Has recent relevant post-qualification experience.*
- *Has sufficient knowledge of the state of the market in the location and category of the tangible fixed asset being valued.*

135. The CoT can make use of either internal or external valuers for the purposes of the revaluation.

136. The CoT will apply its supply chain management polices and procedures when appointing external valuers.

3.1.10.4 Bases of valuation

137. If a policy of revaluation is adopted, the basis of valuation used is 'fair value'.

138. Fair value is defined as the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.

139. The fair value of land and buildings is usually determined from market-based evidence by an appraisal that is normally undertaken by a qualified valuer.

140. The fair value of plant and equipment is usually the market value of the item determined by appraisal.

141. The CoT can apply the income or a replacement cost approach when the items of property, plant and equipment are of a specialised nature and these the items are rarely sold except as part of a continuing business.

142. Specialised property is defined as property that is rarely, if ever, sold in the market, except by way of a sale of the business or entity of which it is part, due to uniqueness arising from its specialised nature and design, its configuration, size, location, or otherwise.

143. The approach applied for the revaluation of assets will be decided by the Chief Financial Officer.

3.1.10.4.1 Depreciated replacement cost (DRC)

144. DRC is defined as the current cost of reproduction or replacement of an asset less deductions for physical deterioration and all relevant forms of obsolescence and optimisation.

145. The depreciated replacement cost (DRC) basis of valuation must be used for specialised items of property, plant and equipment, where there is no means of ascertaining a market value for such assets.

146. Specialised properties might include:

- *Chemical works where the buildings are no more than housings or claddings for highly specialised plant.*
- *Power stations.*
- *Properties of such construction, arrangement, size or specification that there would be no market (for sale to a single owner occupier for continuation of existing use) for the properties.*
- *Standard properties of abnormal size in particular geographic areas that are isolated or remote from main business centres and which are located there for business or operational reasons, such that there is no market there for the properties.*
- *Schools, colleges and research establishments where there is no market for such properties from other competing organisations in the area.*

- *Hospitals, health centres and leisure centres where there is no competing market demand in the area.*
- *Museums, libraries and other similar public sector properties.*

147. *In assessing the DRC of an asset, account should be taken of the age, condition, economic and functional obsolescence and environmental and other factors, including residual value at the end of the asset's useful life.*

148. *The chief financial officer will determine the model that will be applied when using the depreciated replacement cost model.*

3.1.10.4.2 Treatment of accumulated depreciation when tangible assets are revalued

149. *When an item of property, plant and equipment is revalued, accumulated depreciation could be treated in one of two way:*

- *Eliminated against the gross carrying amount of the asset with the net amount restated to equal the revalued amount.*
- *Restated proportionately with the change in the gross carrying amount of the asset such that the net book value of the asset after revaluation equals its revalued amount. This is the method used where an asset is revalued using an index to its depreciated replacement cost.*

150. *The amount of the adjustment to accumulated depreciation forms part of the gain or loss on revaluation.*

151. *The CoT will apply the second method with the respect to the treatment of accumulated depreciation.*

3.1.10.5 Revaluation gains

152. *A revaluation surplus is credited directly to the statement of change in net assets under the heading of revaluation surplus, unless it reverses a revaluation decrease on the same asset previously recognised as an expense, when it should be credited to the profit and loss account to that extent.*

153. *The credit to income should be reduced by subsequent depreciation that would have been charged had the asset not been revalued downwards in the past.*

154. *The revaluation surplus included in the statement of changes in net assets may be transferred directly to retained earnings when the surplus is realised (that is, usually when the asset is derecognised). The transfer is made through reserves and is not made through the profit and loss account.*

155. *The CoT transfers the surplus relating to an asset when the following occurs:*

- *As the asset is used by the CoT, that is, as the surplus is realised;*
- *The asset is retired from use; or*
- *The asset is disposed.*

156. The total amount transferred on an annual basis is the difference between depreciation based on the asset's revalued carrying amount and depreciation based on the asset's original cost. This amount is transferred from revaluation surplus to retained earnings each year, by means of a reserve transfer. This transfer must be authorised by the Chief Financial Officer.

3.1.10.6 Revaluation losses

157. A revaluation decrease should be charged against any related revaluation surplus to the extent that the decrease does not exceed the amount held in the revaluation surplus (that is, in reserves) in respect of that same asset. Any balance of the decrease should then be recognised as an expense in the profit and loss account.

3.1.11 Depreciation

3.1.11.1 General matters

158. The objective to depreciate tangible fixed assets is to reflect in operating profit the cost of use of the tangible fixed assets in the period.

159. The depreciable amount of an asset should be allocated on a systematic basis over its useful life.

160. The method of depreciation that is used should reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.

161. Depreciation charges should be recognised as an expense unless they are included in the carrying amount of another asset.

162. Depreciation applies to all tangible fixed assets, whether held at historical cost or current value, with two exceptions:

- *Investment properties carried as a matter of policy at fair value (as opposed to those carried as a matter of policy at cost) in accordance with IAS 40, 'Investment property', which is not depreciated.*
- *Tangible fixed assets such as most types of land, where it can be demonstrated that depreciation is immaterial.*

3.1.11.2 Definition of depreciation

163. Depreciation is defined as the systematic allocation of the depreciable amount of an asset over its useful life.

164. The depreciable amount is defined as the cost of an asset, or other amount substituted for cost, less its residual value.

165. Depreciation is charged even if an asset that is held at cost less depreciation has a fair value in excess of that carrying amount, so long as the asset's residual value does not exceed its carrying amount.

166. *Repairs and maintenance do not remove the need to depreciate an asset.*

167. *Economic benefits are consumed mainly through the use of an asset.*

168. *However, other factors, such as technical obsolescence and wear and tear whilst an asset remains idle may reduce the economic benefits that might have been obtained from the asset.*

169. *Another factor that might reduce the expected economic benefits is a fall in demand for, or price of, the product produced by the asset.*

170. *The factors to be taken into account when determining the depreciation of a tangible fixed asset, are as follows:*

- *The assets' expected use by the CoT. This is the principal factor and is generally assessed by reference to the asset's expected capacity or physical output.*
- *The assets expected physical deterioration through use or the passing of time (that is, 'wear and tear'), when the asset is both in use and idle. This will depend upon operational factors, such as the number of shifts for which the asset is to be used and on how well the asset is maintained and repaired throughout its life.*
- *Technical or commercial obsolescence. The asset itself or the product or service generated by the asset may become commercially or technically obsolete by being superseded by new or more advanced products or production techniques. Similarly, changes in market demand may render an asset commercially obsolete, for example changes in fads and trends or competitor actions.*
- *Legal or similar limits on the asset's use, for example the expiry of a patent, licence or lease.*

3.1.11.3 Determining the useful life and residual value

171. *Depreciation is calculated by allocating the cost or revalued amount of an item of property, plant and equipment less its estimated residual value (that is, its 'depreciable amount') on a systematic basis over its useful life.*

172. *Depreciation charged in a period is recognised in the statement of financial performance as part of operating profit, unless it is permitted to be included in the carrying amount of another asset.*

173. *This will only occur when depreciation is included in stock or work-in-progress as part of an allocation of overheads, or when it forms part of the cost of a tangible fixed asset.*

174. *Useful life is defined as either:*

- *the period over which an asset is expected to be available for use by an entity; or*
- *the number of production or similar units expected to be obtained from the asset by an entity.*

175. Please refer to CoT's policy on useful life.

176. The estimate of the useful life of an asset is a matter of judgement, based on experience with similar assets.

177. For depreciation purposes land and buildings are treated as separate assets.

178. With some exceptions, such as quarries and landfill sites, land normally has an unlimited useful life and is, therefore, not depreciated.

179. Buildings, however, have a limited useful life and are, therefore, depreciable assets.

180. An increase in the value of land does not affect the determination of the depreciable amount of a building nor remove the need for depreciation to be charged on the building.

181. Where a land asset includes the costs of site dismantling, removal and restoration, the restoration cost part of the land asset is depreciated over the period during which the economic benefits from incurring those costs are obtained. (Please refer to CoT's policy on rehabilitation costs)

182. In some situations the land itself may have a limited useful life in which case it is depreciated over that useful life. An example might be a landfill site that has to be restored. The costs of the obligation to restore the site might be depreciated over the period during which refuse is dumped in the site. The site itself might have a limited useful life to the landfill site operator and its residual value might be considerably less than its original cost. In that case the cost of the land would also be depreciated over the life of the site to its residual value.

183. The depreciable amount of a tangible fixed asset should be allocated on a systematic basis over its useful life.

184. The depreciation method should reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.

185. Useful life means the period over which the asset is expected to be available for use by the entity. This means that depreciation should commence as soon as the asset is acquired and is available for use.

186. Depreciation ceases when an asset is derecognised. Therefore, depreciation does not stop when an asset is idle.

187. However, depreciation will cease to be charged where the asset is classified as held-for-sale. This would be where the asset is available for immediate sale in its present condition and the other conditions in the CoT's policy on "Non-current assets held for sale" have been complied with.

Residual values

188. *Residual value is defined as the estimated amount that the CoT would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.*

189. *Residual values are estimated for an asset as if it were of the age and in the condition expected at the end of its useful life.*

190. *Therefore, the value of the asset in question should be considered at the end of its useful life, but expressed in local currency at the balance sheet date.*

191. *It is therefore, possible that depreciation charged over the useful life to date can actually exceed the depreciable amount when residual values are updated for price changes to the balance sheet date.*

192. *However, in such circumstances the depreciation charge is zero and the over-depreciation is not written back to the statement of financial performance.*

193. *Please refer to CoT's policy on residual value.*

3.1.11.4 Methods of depreciation

194. *There is a variety of acceptable depreciation methods. The method chosen must result in a depreciation charge throughout the asset's useful life and not just towards the end of its useful life or when the asset is falling in value.*

195. *The Chief Financial Officer will determine and implement the method regarded as most appropriate, based on the expected pattern of consumption of future economic benefits, so as to allocate depreciation on a systematic basis over the asset's useful life. This will be communicated as part of the asset management procedures by the Chief Financial Officer.*

3.1.11.5 Depreciation of revalued assets

196. *With the exception of investment properties, depreciation is required to be charged on revalued property, plant and equipment.*

197. *A depreciation charge is made even if the value of an asset exceeds its carrying amount.*

3.1.11.6 Component depreciation

198. *Each part of an item of property, plant and equipment that has a cost that is significant when compared to the total cost of the item, should be depreciated separately.*

199. *Where significant parts of an item of property, plant and equipment have been separately identified they should normally be depreciated separately.*

3.1.11.7 Non-depreciation of certain assets

200. *The useful life of an item of property, plant and equipment cannot be extended without limit by maintenance. This is because the physical life of an item other than non-depreciable land cannot be unlimited. At some point it will be more economic to scrap the physical asset and replace it with a new one.*

201. *On the other hand, for some, exceptional, assets the useful life may be extended to such a degree that any depreciation charge would be immaterial (for example, heritage properties and fine art). Immateriality is the only permissible grounds for not charging depreciation.*

202. *In order to justify that depreciation is immaterial, reasonable assumptions and estimates of useful lives and residual values need to be made.*

203. *In determining whether an asset will not be depreciated, as the associated deprecation is not material, due consideration should be given to the following matters:*

- *A policy of regular maintenance and repair has been implemented such that the item of property, plant and equipment is retained at its previously assessed standard of performance.*
- *The item of property, plant and equipment is unlikely to suffer from technical or commercial obsolescence.*
- *The CoT has implemented a policy of disposing of similar assets well before the end of their useful lives; and*
- *The disposal proceeds of similar assets have not historically been materially less than their carrying values.*

204. *Furthermore, where depreciation is judged to be immaterial the aggregate depreciation should be considered as well as the depreciation on individual assets. This would include considering the effect of cumulative uncharged depreciation on the balance sheet. The depreciation charge and the accumulated depreciation are only immaterial if they would not reasonably influence the decisions of a reader of the financial statements.*

205. *The Chief Financial Officer will designate those items that will not be depreciated as part of the CoT's asset management procedures.*

3.1.11.8 Change in estimate of useful life, residual values and depreciation methods

206. *The useful life, residual values and depreciation methods of assets must be reviewed and assessed on an annual basis.*

207. *The timing for the assessment of the above would be provided by the Chief Financial Officer in terms of CoT's asset management procedures.*

208. *Any change that arises from such review regarded as a change in estimate. This should be dealt with prospectively in terms of "GRAP 3 – Changes in accounting policies, estimates and errors".*

209. *Please refer to CoT's policy on the above documents.*

3.1.12 Impairment of property, plant and equipment

210. *Impairment of property, plant and equipment is dealt with by the CoT's policy on impairments*

211. *The CoT should assess each year whether there is any indication that an asset is impaired. If such an indication exists the entity should estimate the asset's recoverable amount. If the recoverable amount is below the asset's carrying amount, the asset should be written down to its recoverable amount.*

3.1.13 Compensation for impairment

212. *The CoT recognises compensation from third parties when it becomes receivable.*

213. *Compensation from third parties must be included in the statement of financial performance when it becomes receivable.*

214. *Compensation is recognised in the statement of financial performance in accordance with the following principles, that is:*

    - *Income is recognised in the income statement when increase in future economic benefits related to an increase in an asset or a decrease in a liability has arisen that can be measured reliably.*
    - *Expenditure on replacing or restoring the asset should be capitalised. Such expenditure may be incurred either by the entity itself or by the third party (for example the insurance company) that is obliged to compensate for the loss or impairment.*
    - *Property, plant and equipment acquired or constructed to replace impaired or lost assets are recorded initially at cost. It is not acceptable to set up compensation as deferred income, or to deduct such compensation from the acquisition or construction cost of a new asset.*

215. *The above requires that compensation from third parties each event or transaction is regarded as separate and must therefore be accounted for separately as follows:*

    - *Impairments should be accounted for in accordance with impairments policy. (Refer CoT's policy on impairments)*
    - *Derecognition of assets following retirements and disposals should be accounted for as described below.*
    - *Monetary or non-monetary compensation from third parties for items of property, plant and equipment that were impaired, lost or given up should be included in the profit and loss account when receivable.*
    - *The cost of assets restored, purchased or constructed as replacements should be determined under this policy.*

3.1.14 Derecognition of property, plant and equipment

3.1.14.1 General matters

216. *An item of property plant and equipment should be derecognised when:*

- *It is disposed of; or*
- *No future economic benefits are expected from its use or disposal.*

217. *The profit or loss on derecognition (that is, on disposal or retirement from use) of an item of property, plant and equipment is the difference between the estimated net disposal proceeds and the carrying amount.*

218. *The consideration receivable is recognised at fair value. Therefore, if payment is deferred the consideration is recognised at the cash price equivalent. The difference between this figure and the actual amounts receivable is treated as interest receivable over the period of credit given.*

219. *The profit or loss on derecognition should be recognised in the profit and loss account for the period in which derecognition occurs.*

220. *A significant part of an asset may have been identified in accordance with the recognition principles in paragraph 6.3 (component accounting). When such a part is replaced the carrying amount of the old part is derecognised regardless of whether it is separately depreciated.*

221. *The date of disposal of an item of property, plant and equipment may occur in a variety of ways, for example by sale, entering into a finance lease or by donation. The date of disposal is determined using the criteria determined in Generally Accepted Municipal Accounting Practices (GAMAP) 9 (Revenue). The Chief Financial Officer will be responsible for determining the date of disposal.*

3.1.14.2 Intended disposals of property, plant and equipment

222. *Items of property, plant and equipment that are classified as held for sale in terms of the CoT's policy on this matter are excluded from the scope of this policy.*

223. *The conditions that must be met before an asset is classified as held-for-sale are as follows:*

- *The carrying amount of the asset will be recovered principally through a sale transaction rather than through continued use.*
- *The asset must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets.*
- *The sale must be highly probable. For this to be the case management must have committed itself to a plan to sell the asset and initiated and active programme to find a buyer and complete the plan. The asset must be actively marketed for sale at a price that is reasonable in relation to its current fair value. Completion of a sale should be expected within one year from the date of classification as held-for-sale ('the one-year rule'). Actions*

required to complete the sale should indicate that there are unlikely to be significant changes to the plan or that the plan will be withdrawn.

- *There are some circumstances where the 'one-year rule' may be extended. These are where the delay beyond one year is caused by events or circumstances beyond the CoT's control and there is sufficient evidence that the entity remains committed to the sale plan.*

224. *Assets classified as held-for-sale are measured at the lower of their carrying amount and fair value less costs to sell. Any impairment loss on a write down to fair value less costs to sell (if required) is recognised at the point when the asset is reclassified. Depreciation is not charged on assets classified as held-for-sale.*

225. *As reflected above, the conditions that must be met before an asset can be classified as held-for-sale under are quite onerous. Please refer to CoT's policy document on this matter.*

226. *Where the CoT has taken a decision to sell an asset but to be unable to classify it as held-for-sale due all the conditions have not been met, the CoT will account for such asset in accordance with this policy until the conditions in CoT's policy on non-current assets held for sale have been met.*

227. *However, the asset may need to be reviewed for impairment, as a plan to dispose of an asset before the previously expected date is an impairment indicator.*

228. *CoT's policy on non-current assets held for sale excludes items that are to be abandoned or scrapped.*

229. *Assets that are to be abandoned rather than sold must be accounted in accordance with this policy. These assets must be reviewed for impairment as well.*

3.1.15 Disclosures

3.1.15.1 General matters

230. *The disclosure requirements require a table that explains the movements in cost, or revalued amount and depreciation. However, disclosures must be given for each class of property, plant and equipment adopted, which may result in a large volume of disclosures, particularly where a revaluation policy has been adopted.*

231. *In order to meet the disclosure requirements of the GRAP 17 [Property, plant and equipment] the following information should be maintained for each class of property, plant and equipment (for the current and comparative years):*

- *The measurement bases (for example cost or revaluation) used for determining the gross carrying amounts.*
- *The depreciation methods used (for example, straight-line method or declining balance method).*
- *The useful lives or the depreciation rates used.*
- *The gross carrying amount (cost or revalued amount) at both the beginning and end of the period.*
- *The cumulative amount of provisions for depreciation (aggregated with accumulated impairment losses) at the beginning and end of the period.*
- *The depreciation for the period, whether recognised in profit or loss or as part of the cost of other assets.*
- *The carrying amount (that is the net book amount) at the beginning and end of the period.*
- *A reconciliation of the carrying amount at the beginning and end of the period, separately disclosing:*
  - *Additions.*
  - *Assets (or assets included in a disposal group) classified as held-for-sale and other disposals.*
  - *Acquisitions through business combinations.*
  - *Revaluation increases or decreases.*
  - *Impairment losses recognised or reversed directly in equity.*
  - *Impairment losses recognised in the profit and loss account.*
  - *Reversals of past impairment losses written back to the profit and loss account.*
  - *Depreciation.*
  - *Exchange differences arising on the retranslation of the financial statements of a foreign entity.*
  - *Other changes.*

232. *In addition, the comparative information for the above items must be maintained for disclosure in the annual financial statements.*

233. *The financial statements should also disclose:*

- *The existence and amounts of restrictions on title and property, plant and equipment pledged as security for liabilities.*
- *The amount of expenditure included in the carrying amount of property, plant and equipment in the course of construction.*
- *The amount of contractual commitments for the acquisition of property, plant and equipment.*
- *If not separately disclosed on the face of the statement of financial performance, the amount of compensation from third parties for items of property, plant and equipment that were impaired, lost or given up that is included in profit or loss.*

3.1.15.2 Changes in estimates

234. *Details of the nature and amount of a change in accounting estimate that has an effect in the current period or is expected to have an effect in future periods should be disclosed.*

235. *Examples of such changes are changes in respect of:*

- *Residual values.*
- *Estimated cost of dismantling, removing or restoring property, plant and equipment.*
- *Useful lives.*
- *Depreciation methods.*

3.1.15.3 Revalued amounts

236. *Where items of property, plant and equipment are stated at revalued amounts, the information should be maintained for disclosure:*

- *The effective date of the revaluation.*
- *Whether an independent valuer was involved.*
- *The methods and significant assumptions used in estimating fair values.*
- *The extent to which fair values were determined directly by reference to observable prices in an active market or recent market transactions on an arm's length basis or were estimated using other valuation techniques.*
- *The carrying amount of each class of property, plant and equipment determined under the cost model (historical cost less depreciation measurement basis).*
- *The revaluation surplus, showing the change for the period and any restrictions on the distribution of the balance.*
- *The change in the revaluation surplus arising from a change in the liability for decommissioning, restoration or similar liabilities.*

3.1.15.4 Impairment

237. *In addition, disclosures are required in respect of impairment. Please refer to CoT's policy on this matter.*

3.1.15.5 Other matters

238. *The CoT should also maintain the following additional information for disclosure in the annual financial statements*

- *Carrying amount of temporarily idle property, plant and equipment.*
- *Gross carrying amount of any fully depreciated property, plant and equipment that are still in use.*
- *Carrying amount of property, plant and equipment retired from active use and not classified as held-for-sale.*
- *Where the cost model is used, the fair value of property, plant and equipment where this is materially different from the carrying amount.*

3.1.16 Administration issues

239. *Responsibility for recording and updating the asset register in respect of property, plant and equipment rests with the Chief Financial Officer.*

240. *The Chief Financial Officer must ensure that the fixed asset register is updated on a regular basis and that the following information is contained therein:*

- *The date of purchase of an asset or the date the asset was brought into use;*
- *Concise and meaningful description of asset;*
- *The physical location of the asset;*
- *Title deed number (in case of land);*
- *Identification number of asset;*
- *The original cost or fair value;*
- *The most recent revalued value in case of operational land and buildings;*
- *The date and basis of such revaluation;*
- *The accumulated depreciation to date;*
- *The impairment loss to date;*
- *The carrying value;*
- *The rate of depreciation (useful life) and basis of depreciation;*
- *The accumulated maintenance expense required in terms of any maintenance plan in respect of infrastructure assets;*
- *The accumulated maintenance expense incurred to date;*
- *The source of finance*
- *The type of asset (i.e. if we use the asset register to record finance lease assets or investment property, this needs to be specified);*
- *Any relevant insurance arrangement; and*
- *Whether the fixed asset is pledged as security for external loans.*

241. *The Chief Financial Officer must ensure that all assets have unique identification numbers. All movable assets must be marked with barcode labels displaying their assigned asset numbers. It is the responsibility of the cost centre owners to notify the Chief Financial Officer of any assets that are not marked.*

242. *The Chief Financial Officer will ensure that all assets are verified on an annual basis. The Chief Financial Officer, would in terms of the CoT's asset management procedures, provide the timing for the verification of all assets.*

243. *Although custody of an asset rests with the head of a department, the responsibility for classifying property, plant and equipment rests with that Chief Financial Officer.*

244. *The Chief Financial Officer must on an annual basis review the classes of assets and determine the appropriateness of the following:*

- *Measurement basis;*
- *Residual values,*
- *Useful lives;*
- *Classes of assets; and*
- *Basis of valuation (cost or revaluation model).*

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3.2 Heritage assets

We recommend that the existing policy be changed to reflect the following:

3.2.1 Introduction

1. *Heritage assets are those assets that have cultural, environmental or historical significance. Examples of heritage assets include historical buildings and monuments, archaeological sites, conservation areas, nature reserves, works of art, etc.*

2. *Certain characteristics, including the following, are often displayed by heritage assets (although these characteristics are not exclusive to such assets):*

   - *Their value in cultural, environmental, educational and historical terms is unlikely to be fully reflected in a financial value based purely on a market price,*
   - *Legal and/or statutory obligations may impose prohibitions or severe restrictions on disposal by sale,*
   - *They are often irreplaceable and their value may increase over time even if their physical condition deteriorates, and*
   - *It may be difficult to estimate their useful lives, which in some cases could be several hundred years.*

3. *Some heritage assets have service potential other than their heritage value, for example, an historic building being used for office accommodation. In these cases, they may be recognised and measured on the same basis as other items of property, plant and equipment.*

4. *For other heritage assets, their service potential is limited to their heritage characteristics, for example, monuments and ruins. The existence of alternative service potential can affect the choice of measurement base.*

5. *Heritage assets are rarely held for their ability to generate cash inflows, and there may be legal or social obstacles to using them for such purposes.*

3.2.2 Administration issues

6. *Responsibility for recording and updating the asset register, in respect of heritage assets that have been recognised rests with the Chief Financial Officer.*

7. *Although custody of an asset rests with the head of a department, the final the responsibility for identifying heritage assets rests with the Council of City of Tshwane.*

8. *The head of department should ensure that where there is a change in the service potential of a heritage asset, they inform the Chief Financial Officer of this change.*

9. *The classification of an asset as a "heritage asset" should be confirmed by a formal council resolution in order for the CoT to fully accept the costs and responsibilities with regard to the identified heritage asset.*

3.2.3 Disclosure requirements

10. *In order to comply with the disclosure requirements, in respect of heritage assets that have been recognised, the following information must be maintained in the asset register:*

- *the measurement basis used;*
- *the gross carrying amount;*
- *the depreciation method used (if any);*
- *the carrying amount at the beginning and end of the period.*
- *the depreciation during the period (if any) and;*
- *the accumulated depreciation at the beginning and end of the period (if any).*

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3.3 Rehabilitation costs

3.3.1 Introduction

1. *The cost of an asset includes:*

   the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period.

2. *The above costs are referred to as rehabilitation costs*

3. *It may appear odd that the CoT has to capitalise costs that are going to arise much later in the life of asset. However, CoT has an obligation (legal or constructive) to incur these costs at some point as a consequence of acquiring or constructing the asset. Consequently, these costs are just as much part of the cost of acquiring or constructing the asset as the costs incurred at the start of the assets' life.*

4. *Land fill sites, quarries, power stations are examples of where CoT may incur rehabilitation costs. It should be noted that where CoT has to incur rehabilitation costs, the residual value on these assets are regarded to be nil.*

5. *Rehabilitation costs should be identified at the planning and budgeting stage of any project. As stated above, this should be included in the cost of the asset.*

6. *As rehabilitation costs arise much later in the life of an asset, it would be necessary for CoT to raise a provision in respect of these costs. In addition, the provision that needs to be raised must take into account the time value of money.*

3.3.2 Administration issues

7. *Responsibility for recording and updating the asset register with the cost of an asset rests with the Chief Financial Officer.*

8. *Although custody of an asset rests with the head of a department, the responsibility for determining the rehabilitation costs associated with an asset rests with the Chief Financial Officer. Notwithstanding this, heads of departments will be required, on an annual basis, to submit reports (in the format prescribed by Chief Financial Officer) on those assets where rehabilitation costs needs to be provided for. Copies of these reports must be maintained by both head of the department and the Chief Financial Officer.*

9. *Rehabilitation cost of an asset must be assessed as part of the budget process of that asset. These costs must be reviewed on an annual basis by the head of a department. The timing of the review of residual value, useful life and amortisation methods will be determined by the Chief Financial Officer.*

10. *Heads of departments will be required on an annual basis to submit reports (in the format prescribed by the Chief Financial Officer) on the rehabilitation costs of each asset in their custody. Copies of these reports must be maintained by both head of the department and the Chief Financial Officer.*

3.3.3 Rehabilitation costs arising later in the asset's life

11. *Where rehabilitation costs become apparent at a later stage in the life of an asset, for example a change in legislation, these costs should still be capitalised as part of the asset's installation, construction or acquisition costs.*

12. *Provisions in respect of damages that are incurred through the use of the assets' are production costs and not capitalised as part of the cost of the asset. Such costs are part of inventory costs.*

13. *Provisions in respect of wear and tear of a leasehold property, which must be restored at the end of a lease, are costs of using the property and these are not to be capitalised.*

14. *As a general rule, where a change in rehabilitation costs results from new information and developments and does not relate to past periods, this should be accounted for prospectively.*

15. *Where the change in rehabilitation costs does not arise from new information and developments and relates to past periods, this should be accounted for retrospectively.*

3.3.4 Changes in estimates

16. *Generally, it is expected that the cost of rehabilitation will become clearer as time progresses. The way to account for these changes is dependent on the model applied to determine the carrying amount of the asset, that is:*

    - *Cost model; or*
    - *Revaluation model.*

17. *In respect of the cost model – changes in the measuring of rehabilitation costs or the discount rate should be added and deducted from the cost of the related asset subject to the following:*

    - *The amount deducted must not be greater than the asset's carrying amount (that is, we cannot have a negative asset). Where the decrease in the liability exceeds the carrying amount, the excess must be taken to profit and loss.*
    - *If the adjustment increases the cost of the asset (example increase in liability), the responsible head of department must consider whether the revised carrying amount is recoverable. If not, then an impairment test would have to be performed.*

18. *In respect of the revaluation model, the changes are accounted through the revaluation reserve as follows:*

- *Where a revaluation surplus exists, an increase in the liability should be debited against this amount. Any excess should be recognised in the profit and loss.*
- *A decrease in the liability should first be credited to profit and loss to the extent that it reverses any previous revaluation deficit on the same asset that was charged to the profit and loss. Any excess should be credited to the revaluation surplus.*
- *In carrying out the above, where the decrease in the liability exceeds the carrying amount of the asset that would have been recognised had the asset been measured under the cost model, the excess over that cost based on the carrying amount must be recognised in the profit and loss. This is in line with the principal discussed in the previous paragraph, that is, negative assets are not allowed.*

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3.4 *Threshold for movable assets*

3.4.1 Introduction

We recommend that the existing policy be changed to reflect the following:

1. *Threshold capitalisation values are applied to ensure that only items with a material value are capitalised, but are not intended to limit custodial responsibilities for equipment below the threshold. The limit is also to ensure that administration and financial cost to manage non material assets are limited. The threshold value is used to distinguish between property, plant and equipment (as defined in GAMAP 17) that is recorded in the fixed asset register and those that are recognised as an expense (as defined in GRAP 1).*

2. *The basis for the determination of the threshold limit is determined by a number of factors, such as materiality, inflation, CPI, IDP and cost/benefit considerations such as the economical assessment of "future economic benefit considerations" to be derived from the individual asset.*

3. *Certain items must be budgeted for as part of the capital budget, usually as a group of items, even though their acquisition values are below the threshold value and provided the value of the group exceeds the threshold limit. For example, due to their nature and irrespective of the costs to acquire; land, motor vehicles and computer equipment (such as desktops, laptops and printers), are items that must be duly captured on the PPE register when the costs are incurred.*

4. *Subsequent capital costs against an existing network asset must also be capitalised despite its value.*

5. *The threshold value is based on cost price per individual asset. Where the cost of the asset is not available, the fair value of the asset should be applied with respect to applying threshold. The net book value is not considered when applying thresholds.*

6. *The threshold value is only applicable to movable assets.*

7. *Where an item is regarded as falling below the "threshold value", the item is included in the "Inventory Control Systems"*

8. *Responsibility items recorded in the inventory control system (ICS), in respect of record keeping and custody of the assets is delegated to the heads of the departments.*

9. *The threshold value will be reviewed every three years by the Chief Financial Officer and will to coincide with the business planning cycle (IDP and MTEF) during the budget process.*

10. *Changes to the threshold value are regarded as a change in estimate. This should be dealt with prospectively in terms of "GRAP 3 – Changes in accounting policies, estimates and errors".*

11. *The current threshold value is set at R10 000.*

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3.5 Residual value

3.5.1 Introduction

We recommend that the existing policy be changed to reflect the following:

1. *The residual value of an asset refers to the estimated amount that would be obtained from the disposal of the asset, less the cost of disposal. The depreciable amount of the asset is then determined as being the cost of the asset less its residual value.*

2. *Residual value will only be applicable to items with a re-sale value at the end of its expected useful life in an active market. If the asset will be utilised over the physical life as opposed to useful life, any value that will gained on disposal of the asset is considered to be incidental and hence the residual value associated with that asset will be not estimated and recognised.*

3. *An active market is a market where all the following conditions exist:*

   - *The items traded within the market are homogeneous;*
   - *Willing buyers and sellers can normally be found at any time; and*
   - *Prices are available to the public.*

4. *Residual values will only be applicable to the following category of assets:*

   - *Passenger vehicles;*
   - *Busses;*
   - *Service vehicles, excluding specialised vehicles such as ambulances and fire engines;*
   - *Tractors;*
   - *Motor cycles; and*
   - *Light delivery vehicles.*

5. *Residual values will not be applicable to any infrastructure related assets such as electricity and water networks, roads and land and buildings.*

6. *The timing for the assessment of the residual value of an asset would be provided by the Chief Financial Officer in terms of CoT's asset management procedures.*

7. *Responsibility for recording and updating the asset register with the residual value of an asset rests with Chief Financial Officer.*

8. *Although custody of an asset rests with the head of a department, the responsibility for assessing residual value the asset rests with the Chief Financial Officer. Notwithstanding this, heads of departments will be required on an annual basis to submit reports (in the format prescribed by Chief Financial Officer) on the residual value of each asset in their custody. Copies of these reports must be maintained by both head of the department and Chief Financial Officer.*

9. *Residual values should initially be determined as part of the budgeting process and at the recognition date. On acquisition of the asset, information relating to the residual value of an asset must be submitted, to Chief Financial Officer, for updating the asset register.*

10. *The classes of assets to which residual values are applicable should be reviewed on an annual basis. In assessing residual value on assets, due consideration should be given to the following factors:*

    - *Existence of an active market,*
    - *The net value realised on disposal of such assets;*
    - *The repairs and maintenance on the assets to the extent that it increases the useful life of the asset; and*
    - *The actual physical life of the assets in relation to the useful life (Refer to CoT's policy on Useful Life) of the assets, that is, should the asset be used for its physical life, then the residual value will nil as the any proceeds on disposal will be incidental.*

11. *Residual values are determined on an annual basis at year end.*

12. *Changes to the residual value of assets are regarded as a change in estimate. This should be dealt with prospectively in terms of "GRAP 3 – Changes in accounting policies, estimates and errors".*

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3.6 Component accounting

3.6.1 Introduction

1. *The costs related to PPE are recognised at the time they are incurred. This also applies to initial and subsequent costs directly attributable to capitalised assets.*

2. *An asset master record is created for the subsequent asset realised, and all the costs directly related to the asset are capitalised against the master record.*

3. *When reviewing the costs associated for an asset, the following criteria should be considered as this would necessitate the creation of separate master records for the "sub assets":*

   - *Parts of the assets have different useful lives or provide benefits to the CoT in a different pattern;*
   - *Parts of the items of property plant and equipment require replacement at regular intervals;*
   - *The cost being evaluated is significant in relation to the rest of the item of property plant and equipment and can be separately identified from the item of property; or*
   - *The cost of the item of property plant and equipment meets the recognition criteria of an asset.*

4. *All cost over R 10 000 must be evaluated to determine if the costs should be capitalised to the main asset or capitalised as a sub asset.*

5. *Where it is assessed that a separate asset master must be created, the master records will then be linked through specific references created and included in them. These assets will be depreciated on a different basis from the remaining assets.*

6. *In reviewing costs associated with an asset, as a guide, all costs above R 10 000 must be assessed on the above basis. Costs that can not be separately identified from the asset must be included in the total cost of the main asset and be depreciated over the useful life of the main asset.*

7. *It is appropriate to aggregate individually insignificant items such as meters, trolley bins and moulds and to apply the recognition criteria to the aggregate value.*

8. *Responsibility for recording and updating the asset register with the asset components rests with Chief Financial Officer.*

9. *Custody of an asset rests with the head of a department. Consequently, the responsibility for determining the components of an asset rests with that head of department. This should be based on the principles highlighted above and should be done in conjunction with finance department and Chief Financial Officer.*

10. *Notwithstanding the above, it may be necessary to create sub-assets to identify the separate individual assets realised. Each sub-asset's costs may be settled against the individual assets.*

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3.7 Useful life

3.7.1 Introduction

We recommend that the existing policy be changed to reflect the following:

1. *Useful life is a key factor in setting the period over which an asset will be depreciated.*

2. *Useful life represents the period over which CoT will use the asset and is determined as part of the budgeting process for the acquisition of assets. This may differ from the actual life of an asset, for example, CoT may replace its fleet of motor vehicles every seven years, notwithstanding the fact that these vehicles could last a period of ten years. In this example, the useful life of the asset is seven years while the actual life of the asset is ten years.*

3. *Useful life is defined as: "the period of time over which an asset is expected to be used by the CoT, or the number of production or similar units expected to be obtained from the asset by the CoT."*

4. *The useful life of an asset must be reviewed and updated on annual basis, that is, an assessment of the remaining useful life would have to be performed on an annual basis.*

5. *The timing for the assessment of the useful life of an asset would be provided by the Chief Financial Officer in terms of CoT's asset management procedures.*

6. *Responsibility for recording and updating the asset register with the useful life and remaining useful life of an asset rests with Chief Financial Officer.*

7. *Although custody of an asset rests with the head of a department, the responsibility for assessing the useful life the asset rests with the Chief Financial Officer. Notwithstanding this, heads of departments will be required on an annual basis to submit reports (in the format prescribed by Chief Financial Officer) on the useful life of each asset in their custody. Copies of these reports must be maintained by both head of the department and the Chief Financial Officer.*

8. *In assessing the useful life of an asset, the following factors must be considered:*

   - *The period that the CoT expects to gain service potential from the asset.*
   - *The ability to redeploy the asset within the CoT over time.*
   - *Whether the asset has been acquired for a specific project.*
   - *The past experience of such assets in use and the appropriateness of this given the technology embedded in the asset.*
   - *Any assessment performed by an independent advisor on the condition of the asset or its expected life expectancy.*
   - *The opinion of the user or relevant expert about the assets "useful life".*
   - *In addition, consideration should be given to the repairs and maintenance policy in assessing the useful life of an asset.*

- *Other factors that will impact on the remaining useful life of the asset.*
- *Decisions taken by council that would affect the useful life of the asset*
- *Decision taken by external parties (for example, National Government) that would affect the useful life of an asset.*

9. *The useful life of an asset must be considered as part of the budgeting process of an asset. On acquisition of the asset, information relating to the useful life of an asset must be submitted, to Chief Financial Officer, for updating the asset register.*

10. *Changes to the useful life of assets are regarded as a change in estimate. This should be dealt with prospectively in terms of "GRAP 3 – Changes in accounting policies, estimates and errors".*

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3.8 Subsequent expenditure on assets

3.8.1 Introduction

We recommend that the existing policy be changed to reflect the following:

1. *Repairs and maintenance are those costs incurred in the normal day to day maintenance of an item.*

2. *It is sometimes difficult to distinguish whether subsequent expenditure should be expensed or capitalised.*

3. *In respect of the budgeting process, repairs and maintenance is accounted for as part of the operating budget while those expenditures that are capitalised are part of the capital budget.*

3.8.2 Recognition

4. *Subsequent costs should be capitalised only if they meet the following criteria:*

   - *It is probable that future economic benefits associated with the item will flow to the entity; and*
   - *The cost of the item can be measured reliably.*

5. *Subsequent expenditure on an item of property, plant and equipment shall be added to the carrying amount of the asset when it is probable that future economic benefits or service potential over the total life of the asset is in excess of the most recently assessed standard of performance of the existing asset.*

6. *Examples of improvements that result in increased future economic benefits or service potential include the following:*

   - *Modification of an item of plant to extend its useful life, including an increase in its capacity,*
   - *Upgrading machine parts to achieve a substantial improvement in the quality of output, and*
   - *Rehabilitation of a road enabling a substantial reduction in previously assessed maintenance costs.*

7. *All other subsequent expenditure shall be recognised as an expense in the period in which it is incurred.*

8. *Expenditure related to repairs or maintenance of property, plant and equipment are made to restore or maintain the future economic benefits or service potential that CoT can expect from the asset. It does not increase the performance of the asset beyond the most recently assessed standard of performance of the asset. As such, they are usually recognised as an expense when incurred. For example, the cost of servicing or overhauling plant and equipment is usually an expense since it restores, rather than increases, the most recently assessed standard of performance.*

9. *Furthermore, the capitalisation or expensing of subsequent expenditure with respect to an item of property, plant and equipment will depend on the circumstances which were taken into account on the initial measurement and recognition of the related item of property, plant and equipment and whether the subsequent expenditure is recoverable.*

10. *For example, when the carrying amount of an item of property, plant and equipment already takes into account a loss in economic benefits or service potential, the subsequent expenditure to restore the future economic benefits or service potential expected from the asset can be capitalised, provided that the carrying amount does not exceed the total economic benefits or service potential that CoT expects to recover from the continued use and ultimate disposal of the item.*

11. *This is also the case when the purchase price of an asset already reflects CoT's obligation to incur expenditure in the future, which is necessary to bring the asset to its working condition. An example of this might be the acquisition of a building requiring renovation. In such circumstances, the subsequent expenditure is added to the carrying amount of the asset to the extent that it can be recovered from future use of the asset.*

12. *Major components of some items of property, plant and equipment may require replacement at regular intervals. For example, a reservoir may require relining after a specified number of hours of usage or components of a sewerage purification works may require replacing during the lifetime of the works, or a road may require resurfacing every few years, a furnace may require relining after a specified number of hours of usage. These components should be recognised for as separate assets as their useful lives differ from those of the items of property, plant and equipment to which they relate. Therefore, provided the recognition criteria is satisfied, the expenditure incurred in replacing or renewing the component is accounted for as the acquisition of a separate asset and the replaced asset is written off.*

13. *The costs of the day-to-day servicing of the item is not capitalised to the carrying amount of an item of property, plant and equipment. These costs do not give rise to increased future economic benefits in a specific asset itself but rather maintains the standard of the asset item. These costs are expensed when incurred.*

14. *Costs of day-to-day servicing are primarily the costs of labour and consumables, and may include the cost of small parts. These costs are often described as 'repairs and maintenance' in respect of the item of property, plant and equipment.*

15. *In deciding whether subsequent expenditure should be capitalised a point of reference is required. This is determined at the time of acquisition and as part of the budgeting process. Prior to an asset being acquired, an assessment must be made of the standard of performance expected from it, in order to determine the appropriate useful life, residual value and depreciation method to be used. As part of this assessment it will be expected that there will be certain future costs associated with the asset in order to keep the asset in a good enough condition to achieve that expected level of performance. These costs are routine maintenance and repairs.*