AP 531 - TANGIBLE CAPITAL ASSETS

BACKGROUND

Saskatoon Public Schools (SPS) is required to report tangible capital assets (TCA) in accordance with standards issued by The Public Sector Accounting Board (PSAB), section PS 3150 published in The CPA Canada Public Sector Accounting Handbook and reporting guidelines set by the Ministry of Education.

This procedure provides information for accounting and reporting for:

- owned tangible capital assets
- construction projects in progress
- leased tangible capital assets

DEFINITIONS

Amortization- is the accounting process of allocating the costs less the residual value of a TCA to operating periods as an expense over the useful life in a rational and systematic manner appropriate to its nature and use.

Betterment – is a cost incurred to enhance the service potential of a TCA. Service potential may be enhanced where there is an increased capacity to provide services.

In accordance with Ministry of Education guidance, betterments would be capitalized only if:

- the project is a new build or includes the addition of space to the asset (i.e. new building or relocatable)

Costs that restore the TCA to working condition and does not add space would be expensed. Examples of costs that would be expensed include:

- replacing carpeting/flooring
- roof repair/replacement
- boiler repair/replacement
- heating, ventilation, and air conditioning systems
- repairs to restore assets damaged by fire, flood, accident or similar events, to the condition just prior to the event. Any money received from insurance is to be used to offset the unexpected cost
- electrical upgrades
- painting

Cost – of an asset is the amount of consideration given up to acquire, construct, develop or better an asset and includes all costs directly attributable to acquisition, construction, development or betterment of the asset including installing the asset at the location and in the condition necessary for its intended use. Cost also includes the asset retirement cost accounted for in accordance with asset retirement obligations in PS 3280. The cost of a tangible capital asset includes:

- purchase price of the asset
- installation costs
- design and engineering fees
- legal fees
- survey costs
- site preparation costs
- freight charges
- transportation insurance costs
- duties
- direct construction or development costs (materials and labour)
- costs directly attributable to the construction or development activity
- betterments

Disposal – refers to the removal of a capital asset from service because of a sale, destruction, loss or abandonment.

Fair Market Value – is the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable and willing parties (buyer and seller).

Furniture and equipment - includes fixed or moveable tangible capital assets to be used for operations, the benefits of which extend beyond one year from the date of receipt

Impairment – occurs when conditions indicate that a tangible capital asset no longer contributes to the ability to provide goods and services, or that the value of future economic benefits associated with the tangible capital asset is less than its net book value.

Land – is the surface that is used to support structures and purchased or acquired for building sites and other program use but not land held for resale. Land normally has an unlimited life and is not amortized.

Land Improvements – consist of betterments and site preparation that ready land for its intended use such as parking lots, landscaping and fencing and are usually exhaustible and amortized.

Leased Capital Assets - are TCA leased by the division for use in the delivery of goods and services. Substantially all of the benefits and risks of ownership are transferred to the division without requiring the transfer of legal ownership.

Net Book Value – of a tangible capital asset is its cost, less accumulated amortization and the amount of any write-downs.

Non-financial Assets - include TCA and other assets such as prepaid expenses and inventories of supplies. Non-financial assets are acquired, constructed or developed assets that are normally employed to deliver division services, may be consumed in the normal course of operations and are not for sale in the normal course of operations.

Repairs and Maintenance - are reoccurring expenditures, periodically or regularly required as part of the anticipated schedule of works required to ensure that the asset achieves its useful life. It is an expenditure that keeps an asset in a condition that helps maintain or ensure realization of the future economic benefits that are expected from the asset over its initially useful life.

Residual Value – is the estimated net realizable value of a capital asset at the end of its estimated useful life. A related term, salvage value, refers to the realizable value at the end of an asset's life. If the division expects to use a capital asset for its full life, residual and salvage value are the same.

Straight-line Method – is amortization that allocates the costs less estimated residual value of a capital asset over each year of its estimated useful life.

Tangible Capital Assets (TCA) – are non-financial assets having physical substance that are acquired, constructed or developed and

- are held for use in the production or supply of goods and services, for rental to others, for administrative purposes or for the development, construction, maintenance or repair of other TCA;
- have useful lives extending beyond an accounting period (the fiscal year);
- are to be used on a continuing basis; and
- are not intended for sale in the ordinary course of operations.

Technology- includes computers and consists of hardware and software that can be considered a component of, is typically attached to, or communicates with an information system. The term encompasses such things as: processing units, memory apparatus, input and output devices, connectivity equipment, networking equipment, printer and copiers.

Useful Life – is the estimate of the period over which it is expected to be used as a tangible capital asset.

Work in Progress – is the accumulation of capital costs for partially constructed or developed projects.

Works of Art and Historical Treasurers – are property that has cultural, aesthetic, or historical value that is worth preserving perpetually. These assets are not recognized as TCA because a reasonable estimate of the future benefits associated with such property cannot be made. The existence of such property is disclosed.

Write-Down – is a reduction in the cost of a capital asset as a result of a decrease in the quality or quantity of its service potential. A write-down should be recorded and expensed in the period the decrease can be measured and is expected to be permanent.

PROCEDURES

MEASUREMENT

TCA that meet the criteria for capitalization are capitalized and recorded at cost.

The cost is recorded as amortization over the useful life of the tangible capital asset.

TCA that meet the criteria for capitalization may be gifted or contributed by an external third party with no cash outlay. Where an asset is acquired at no cost or for nominal value, the amount is recorded at fair market value at the acquisition date. Fair market value is estimated using market or appraised values. When an estimate of fair market value cannot be reasonably estimated, the asset will be recognized as its nominal value.

CAPITALIZATION APPROACHES

Individual asset approach

Under the individual asset approach, TCA purchases are tracked, capitalized, and amortized as an individual asset until the date in which they are fully amortized and/or disposed of.

The individual asset approach is used for the following asset classes:

- land
- land improvements
- buildings

Buildings consist of several components (frame, roof, HVAC). Each component of the building is not recorded and accounted for as a separate asset due to the cost versus the benefit of collecting and maintaining it. The building is recorded and accounted for as a single individual asset.

Pooled cost approach

Under the pooled cost approach, all costs are pooled and capitalized under the applicable tangible capital asset class; costs are not tracked by individual asset.

TCA recorded under the pooled cost approach are to be tracked by year of purchase in the applicable tangible capital asset class.

TCA recorded using the pooled cost approach will have a deemed disposal at the end of their useful life; individual disposals are not generally recorded.

If an asset is sold or disposed of before the asset has reached the end of its useful life, the proceeds (if any) are to be recorded as revenue.

Even though detailed inventory records may not be required for financial statement purposes; departments within the organization are encouraged to maintain inventory records for management purposes where it makes sense to do so (i.e. IT department maintains equipment inventory, with attention given to repairs and service calls made on individual pieces of equipment).

The pooled assets approach will be used on:

- Furnishings and equipment
- Computer hardware and networking equipment
- Computer software
- Vehicles
- Relocatables

AMORTIZATION

1. A straight-line method of amortization should be used for all asset classes.
2. Straight-line method is amortization that allocates the costs less estimated residual value of a capital asset over each year of its estimated useful life.
3. For major projects lasting greater than one year, costs are accumulated as work in progress. Work in progress is not amortized. Work in progress should be transferred to a tangible capital asset once the architect, engineer or consultant has issued the certificate of substantial completion; providing evidence that the asset has met engineering and safety standard and is ready to be placed into service or occupied. Examples of work in progress are the construction of a new school or relocatable addition.
4. A full year of amortization will be taken in the year of purchase regardless of when this event occurs in the fiscal year.
5. There will be no residual value attached to buildings for amortization purposes. Based on past transactions, property has generally sold for the value of the land with nominal value attached to the building.
6. Fully amortized single asset buildings will remain on the books until such time as the assets are disposed of.

CAPITAL LEASES

Capital leases are a means of financing the acquisition of a capital asset where the lessee carries substantially all of the risks and benefits of ownership. Capital leases are recorded as if the lessee had acquired the tangible capital asset and assumed liability. Capital leases are amortized over the period of expected use of the asset. If the lease contains terms that allow ownership to pass to SPS as a bargain purchase option, the period of amortization is the economic life of the property. Otherwise, the property is amortized over the lease term.

If one or more of the following criteria exists, the lease should be accounted for as a capital lease:

- There is reasonable assurance that the division will obtain ownership at the end of the lease;
- The lease term is equal to a major potion (75% or more) of the estimated economic life of the leased property
- Financing payments substantially cover (90% or more) the fair value cost of the leased property.

A lease which does not meet any of the above criteria should be accounted for as an operating lease. No asset or liability is recorded and the monthly payment is expensed over the lease term.

TRADE IN

A trade in occurs when assets such as a vehicle or computer equipment is disposed of and replaced with a new asset through the same supplier in the same transaction. This transaction should be accounted for as two separate entries. Because vehicles and computer equipment are recorded as pooled assets; the full trade-in value is to be recorded as revenue. The new asset acquired is recorded at its full cost; trade in value for the old asset does not affect the cost of the new asset.

DISPOSAL

TCA recorded using the pooled approach will have a deemed disposal at the end of their useful life; individual disposals <u>are not generally</u> recorded.

This deemed disposition takes place the year following the final year in which amortization is posted for the asset pool. On disposal of an asset, the historical cost and accumulated amortization must be removed from the books.

Buildings are recorded as single assets and their disposal treatment is different than that used for pooled assets. When buildings are disposed of as a result of sale, destruction or abandonment; the cost and the accumulated amortization is removed from the accounting records and any gain or loss is recorded at that time. Costs that are associated with the disposal are expensed.

A gain or loss on disposal is the difference between the net proceeds received and the net book value of the building and is accounted for as a revenue or expense, respectively, in the period the disposal occurs.

WRITE-DOWNS

In accordance with PSAB 3150.31-34, a capital asset should be written down when an asset no longer contributes to providing services and the reduction is expected to be permanent. The cost of the TCA should be reduced to reflect the decline in the asset`s value. Write downs of capital assets should be accounted for as an expense in the current period. Annual amortization of an asset that has been written down should be calculated using the net book value after the write down and the remaining estimated useful life. Conditions that indicate a write down is necessary may include:

- Change in the manner or extent to which the asset is used;
- Removal of the asset from service.
- Physical damage.
- Significant technological development.
- A change in the law or environment affecting the extent to which the asset can be used.
- A decline in, or cessation of the need for the service provided by the asset.
- A decision to halt construction of the asset before it is complete or in a useable or saleable condition

SCHEDULE OF ASSET CLASSIFICATIONS, THRESHOLDS AND USEFUL LIVES

The table below outlines the classification, threshold and estimated useful life application to each asset category. A threshold of “All” means that all capital asset purchases, regardless of cost, are recorded.

Capital Asset Class and Category	Threshold	Tracking Method	Useful Life Years	Amortization
Land and land improvements				
Land	All	By asset	Indefinite	n/a
Land Improvements	$100,000*	By asset	20 years	Straight-line
Buildings and building betterments				
Buildings	All	By asset	50 years	Straight-line
Building short term (portables, storage sheds, out buildings, garages)	All	Pooled	20 years	Straight-line
Vehicles				
Heavy Vehicles (e.g graders and tractors)	$ 10,000	Pooled	10 years	Straight-line
Trucks, vans and cars	$ 10,000	Pooled	5 years	Straight-line
Office and Information Technology				
Computer Hardware				
IS department account lines (system)	$10,000**	Pooled	5 years	Straight-line
Annual school account lines	N/A	Expensed	N/A	N/A
Computer Software				
IS department account lines (system)	$10,000**	Pooled	5 years	Straight-line
Annual school account lines	N/A	Expensed	N/A	N/A
Furniture and Equipment			10 years	Straight-line
Purchases for new school start up or major renovation/addition	All**	Pooled	10 years	Straight-line
Annual school account lines	N/A	Expensed	N/A	N/A

* Land improvements includes playgrounds (which are typically donation funded). The ministry threshold set for this category is $25,000. Due to materiality considerations, SPS has set a minimum threshold of $100,000.

**The minimum threshold set by the Ministry of Education for furniture and equipment and computer hardware and software is $1,000. Due to materiality considerations, SPS has set a minimum threshold of $10,000.

Schools are allocated budgets which can be used to supplement or replace existing furniture, equipment, musical instruments, science equipment, AV equipment, computers, sports equipment etc. These purchases would typically be under $1,000, but from time to time could exceed that threshold. In addition, in kind gifts such as music equipment are received and from time to time could exceed the threshold of $1,000. The value of these purchases or in kind gifts would not be significant. All such items will be expensed.

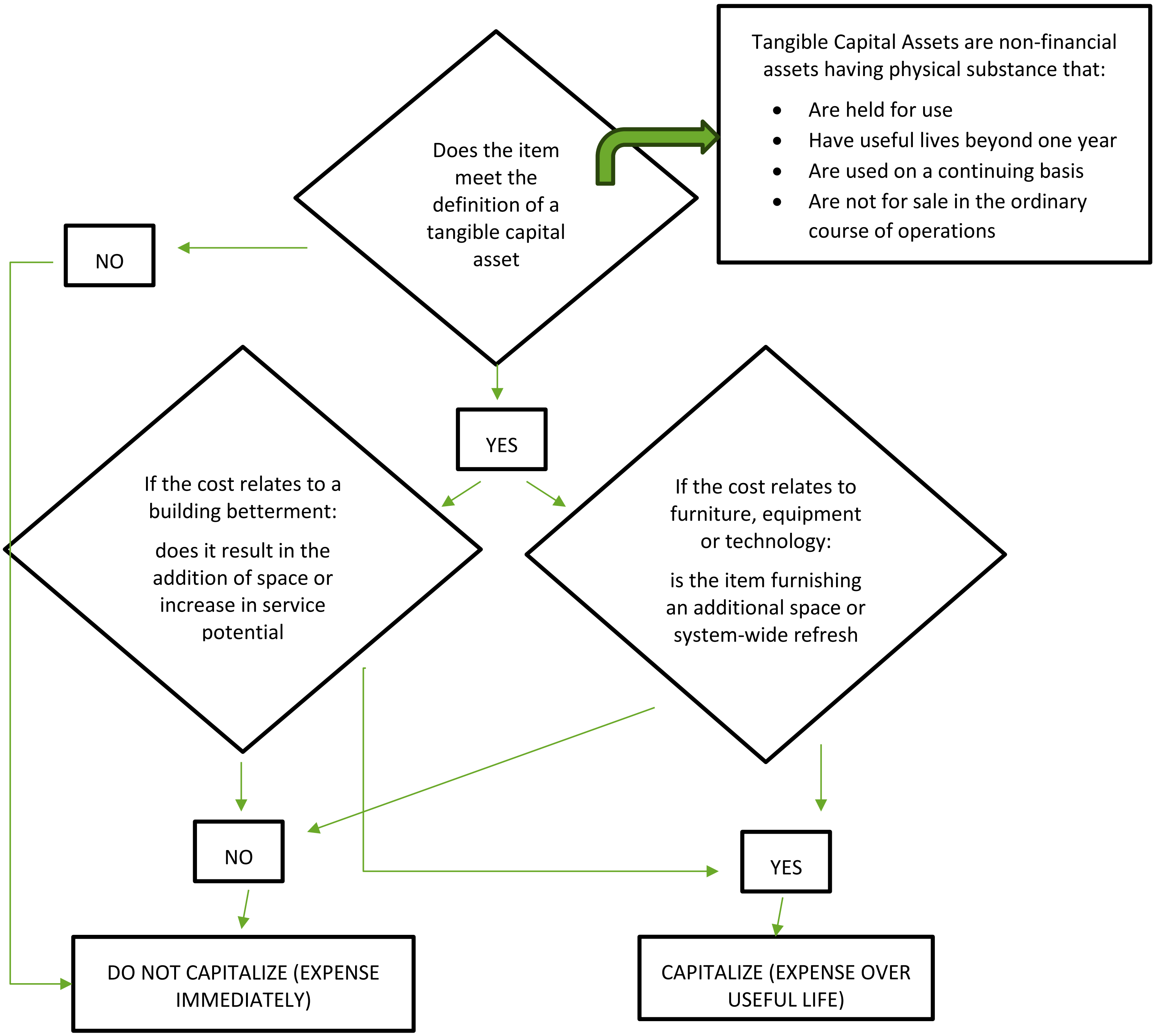
The centralized departments of the division will also make purchases of furniture and equipment and technology for system-wide refresh initiatives. Furniture, equipment and technology will be capitalized as pooled assets in the following situations even though from time to time the individual asset may be under $1,000:

- Major renovation of a building in which new FE&T is included to replace the existing items;
- Hardware and software budgets managed by the chief technology officer (for example technology refresh projects).
- Construction of a new building;
- Construction of a building addition that includes new FE&T;
- Major furniture replacement initiatives (for example a system-wide refresh).
- Special education furniture greater than $1,000

All other centralized departments of the division that make purchases of furniture and equipment which would be recorded at cost or are gifted TCA which would be recorded at fair market value on an ad-hoc basis will be expensed. These purchases would typically be under $1,000, but from time to time could exceed that threshold.

APPENDIX A - CRITERIA FOR CAPITALIZATION

Below is a decision tree to determine whether a cost related to a building betterment and a cost related to furniture, equipment or technology should be capitalized or expensed.



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