County of Lethbridge Policy Handbook

EFFECTIVE: **October 15, 2009** **SECTION: 100 NO. 150 Pg 1 of 17**

APPROVED BY: **County Council** **SUBJECT: Tangible Capital Assets**

REVISED DATE:

AUTHORITY, PURPOSE AND SCOPE

The County of Lethbridge recognizes the importance of having capital policies in place to achieve consistent recording of tangible capital assets, and to assist with the preparation of financial statements that will comply with generally accepted accounting principles. The purpose of this policy is to provide direction to all departments for recognizing and recording Tangible Capital Assets in accordance with Public Sector Accounting Board (PSAB) 3150.

Department Supervisors are responsible to ensure that their Capital Asset Listings are accurate and complete. Each department is responsible for the proper use, care and maintenance of their tangible capital assets.

The Finance Department is responsible to account for and report tangible capital assets in the County's annual financial statements. This requires all departments to effectively communicate and share information on tangible capital assets. Director of Corporate Services is to review accounting transactions to ensure compliance with this policy.

Amortization methods and estimated useful life should be reviewed by the Finance Department and Department Supervisors on a regular basis and revised when appropriate and necessary. Capital projects should be reviewed to determine any capitalization requirements.

EFFECTIVE DATE

This policy is effective January 1, 2009 and applies to all tangible capital assets that exist at that time and acquired thereafter.

DEFINITIONS AND CLASSIFICATION OF ASSETS

Inventory – purchases made for resale or intended to be consumed in the delivery of programs, core services or activities. Examples would be gravel stockpiles, equipment parts, fuel, oil, tires, grader blades, etc.

Operating Expenditures – purchased supplies or services that are consumed in the delivery of programs or services. These costs are charged directly to the Statement of Operations in the year in which they were incurred. Examples would be professional fees, utility charges, insurance, office supplies, etc.

Tangible Capital Assets – non-financial assets, including betterments, having physical substance that:

- are in excess of the capitalization thresholds set out in this policy;
- are held for use in the production or supply of goods and services, for rental to others, for administrative purposes or for the development, construction, maintenance or repair of other tangible capital assets;
- have useful economic lives extending beyond the current accounting period;
- are to be used on a continuing basis; and
- are not for sale in the ordinary course of operations.

Major Classifications of Tangible Capital Assets ***(see Appendix A for detailed list)***

1. Land
   Land includes land purchased, contributed or acquired for value for parks and recreation, building sites, infrastructure (highways, dams, bridges, tunnels, etc.) and other program use, but not land held for resale.

2. Land improvements
   All improvements of a permanent nature to land such as parking lots, landscaping, lighting, pathways, and fences.

3. Buildings
   Permanent, temporary or portable building structures, including but not limited to offices, garages, warehouses, and recreation facilities intended to shelter persons and/or goods, machinery, equipment and working space.

4. Engineered structures *(further broken down into minor asset classifications)*
   Permanent structural works such as roads, bridges, canals, dams, water and sewer, and utility distribution and transmission systems, including plants and substations.

   a) Roadway system
      Assets intended for the direct purpose of vehicle or pedestrian travel or to aid in vehicle or pedestrian travel. Includes roads, bridges, overpasses, ramps, parkades, lights, sidewalks and signage.

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b) Water systems
Systems for the provision of water through pipes or other constructed convey. It is normally comprised of assets for the intake, distribution, storage and treatment of safe potable water. It may also be comprised of assets required to distribute non-potable water. Includes mains, services, pump and lift stations, plants and equipment, reservoirs and fire hydrants.

c) Wastewater systems
Wastewater is defined as water that has been used for household, business and other purposes, which flows from private plumbing systems to public sanitary sewers and on to a treatment plant. This system is comprised of assets used for the collection and treatment of non-potable water intended for return to a natural water system or other originating water source or used for other environmentally approved purposes. Includes mains, services, pump and lift stations, plants and equipment, and lagoons.

d) Storm system
Assets used for the collection, storage and transfer of water as a result of rain, flood or other external source to a natural water system. Includes mains, services, catch basins, pump and lift stations, outfalls and retention ponds.

5. Machinery and equipment
Equipment that is heavy equipment for constructing infrastructure, smaller equipment in buildings and offices, furnishings, computer hardware and software. This class does not include stationary equipment used in the engineered structures class.

6. Vehicles
Rolling stock that is used primarily for transportation of goods or individuals.

7. Cultural and historical assets
Works of art and historical treasures that have cultural, aesthetic or historical value that are worth preserving perpetually. These assets are not recognized as tangible capital assets in the financial statements, but the existence of such property should be disclosed. Buildings declared as heritage sites may be included in this asset classification.

Amortization
The cost, less any residual value, of a tangible capital asset with a limited life should be amortized over its useful life in a rational and systematic manner appropriate to its nature and use by the government.

The amortization of the costs of tangible capital assets should be accounted for as an expense in the statement of operations.

Betterment
Subsequent expenditures on a tangible capital assets that enhance their service potential. Service potential may be enhanced when there is an increase in the previously assessed physical output or service capacity, where associated operating costs are lowered, the useful life of the property is extended or the quality of the output is improved.

Capital Lease
A capital lease is a lease with contractual terms that substantially transfers all the benefits and risks inherent of property ownership to the County. This normally occurs when one or more of the following conditions are present at the inception of the lease:

a) There is reasonable assurance that the County will obtain ownership of the lease property by the end of the lease term.

b) The lease term is of such duration that the County will receive substantially all of the economic benefits expected to be derived from the use of the leased property over its lifespan.

c) The lessor would be assured of recovering the investment in the leased property and of earning a return on the investment as a result of the lease agreement.

Cost
The gross amount of consideration given up to acquire, construct, develop or better a tangible capital asset, and includes all costs directly attributable to acquisition, construction, development or betterment of the tangible capital asset, including installing the asset at the location and in the condition necessary for its intended use.

The cost of a contributed tangible capital asset, including a tangible capital asset in lieu of a developer charge, is considered to be equal to its fair value at the date of contribution. Capital grants would not be netted against the cost of the related tangible capital asset.

The value of a leased tangible capital asset is determined in accordance with the Public Sector Accounting Board's Guideline 2, Leased Tangible Capital Assets (PSG-2):

> Property that meets the definition of a leased tangible capital asset is accounted for as both a tangible capital asset and a liability.
>
> The value of the leased tangible capital asset and the amount of the lease liability, recorded at the beginning of the lease term, would be the present value of the minimum lease payments, excluding the portion relating to executory costs (costs related to the operation of the leased tangible capital asset; e.g., insurance, maintenance cost and property taxes).
>
> At inception of the lease, the estimate of the discount rate used should be reviewed together with:
>
> - the present value of the minimum lease payments;
> - the assumed fair value of the property; and
> - the assumed residual value, to ensure that all figures are reasonable and internally consistent.
>
> The discount rate for determining the present value of the minimum lease payments would be the lower of the local government's rate for incremental borrowing and the interest rate implicit in the lease. The maximum value recorded for the asset may not, however, exceed the leased property's fair value.
>
> A leased tangible capital asset would be amortized over the period of its expected use, on a basis consistent with the local government's amortization policy for similar tangible capital assets. If the lease contains terms that allow ownership to pass to the local government, or a bargain purchase option, the period of amortization would be the economic life of the property. Otherwise, the property would be amortized over the lease term. Lease payments would be allocated

between repayments of the liability, interest expense and any related executory costs.

The total minimum lease payments, less the initial liability recorded, represents the total interest cost of the lease. The interest expenditure/expense would be calculated based on the same discount rate used in computing the present value of the minimum lease payments applied to the outstanding lease liability at the beginning of the lease payment period.

Fair Value
The amount of the consideration that would be agreed upon in an arm's length transactions between knowledgeable, willing parties who are under no compulsion to act.

Maintenance and Repairs
Expenditure made to maintain the predetermined service potential of a tangible capital asset for a given useful life. Such expenditures are charged in the accounting period in which they are made.

Net Book Value
Cost, less both accumulated amortization and the amount of any write-downs.

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

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

Useful Life
The estimate of either the period over which a tangible capital asset is expected to be used by a government, or the number of production or similar units that can be obtained from the tangible capital asset by a government. The life of a tangible capital asset may extend beyond the useful life of a tangible capital asset to a government. The life of a tangible capital asset, other than land, is finite, and is normally the shortest of the physical, technological, commercial and legal life.

Write-down
A reduction in the cost of a tangible capital asset to reflect the decline in the asset's value due to an impairment that is considered other than temporary.

RECORDING AND VALUING ASSETS

Recording the Assets

The Finance Department in conjunction with all departments will ensure that all tangible capital assets held by the department at the date this policy becomes effective and any future acquisitions of tangible capital assets are properly valued and recorded.

- Ensure that all costs required to make a capital asset operational have been recorded in the appropriate capital account. Costs include purchase price and other acquisition costs such as installation costs, design and engineering fees, legal fees, survey costs, site preparation costs, freight charges, transportation insurance costs and duties.

- The cost of a constructed asset would normally include direct construction or development costs (such as materials and labour), and overhead costs directly attributable to the construction or development activity (such as the costs of leased space used solely for the construction or development activities);

- The County of Lethbridge will not capitalize interest costs on tangible capital assets.

- Ensure that procedures are in place to differentiate between "betterments" which are capitalized, and "repairs and maintenance" which are expensed. Betterments improve the functionality or increase the useful life of an asset while repairs and maintenance primarily maintain the functionality of the asset. Where a cost can not easily be differentiated between a repair and a betterment, the cost should be expensed in respecting the accounting principle of conservatism;

- Establish procedures to ensure that when tangible capital assets are sold or traded-in, the historical cost and accumulated amortization amounts relating to the particular capital asset are removed from the appropriate general ledger accounts and a gain or loss on disposal is recognized to the extent that the asset's net book value differs from the sale proceeds or from the trade-in value;

- Establish procedures to distinguish between a capital lease and an operating lease;

- Establish procedures to ensure that when tangible capital assets become obsolete, impaired and/or are removed from service, and the long-term expectation is that the assets no longer have value or use to the County, finance will write down the net carrying amount of the asset to its net realizable value. If the capital asset is subsequently returned to service the asset can not be increased to its prior book value. Only betterments that have been made to bring the asset back into service should be added to the book value;

- Estimate the useful life of tangible capital assets on a consistent basis.

Valuing the Assets

All tangible capital assets held by a department at the date this policy becomes effective must be identified and valued using an appropriate cost base.

Where practical and cost-effective, existing tangible capital assets will be valued using historical costs, adjusted for the proportion of the useful life of the asset that has already been consumed through the establishment of a provision for accumulated amortization.

Where it is not practical and cost-effective to establish a reasonable estimate of an asset's historical cost, replacement value will be used and extrapolated back to estimated historical cost using the consumer price index (CPI) or some other relevant price/cost index.

All lease agreements must be reviewed to determine if they should be accounted for as capital leases or operating leases.

Donated assets should be valued at fair value at the date of construction or contribution. Fair value may be determined using market or appraisal values. If the fair value cannot be determined, the asset should be recorded at a nominal value (one dollar), however this would be extremely rare.

Grouping of Assets (Whole Asset vs. Component Approach)

For purposes of capitalization and amortization, the two methods of defining a capital asset are Whole Asset and Component.

- The Whole Asset approach considers an asset to be an assembly of connected parts. Costs of all parts would be capitalized and amortized as one asset. For example, a computer network would be considered as one asset.

- Under the Component approach, different components are individually capitalized and amortized. Under this approach, the servers, routers, lines, software, etc. used in a network would all be individual assets.

The whole asset method and the component approach are equally acceptable under Generally Accepted Accounting Principles. In certain circumstances, it is appropriate to allocate the total disbursement on an asset to its component parts and account for each component separately. This is the case when the component assets have different useful lives or provide economic benefits or service potential to the County of Lethbridge in a different pattern, thus necessitating use of different amortization rates.

For example, the pavement, curbs, sidewalks, bridges and lighting may need to be treated as separate items within a road system to the extent that they have different useful lives. Similarly, the furnace, air conditioning system, roof and structure of a building may need to be treated as separate amortizable assets if they have different useful lives.

Additional factors influencing the choice of method include:

- Significance of amounts;
- Quantity of individual asset components (volume);
- Availability of information with respect to specific components of the capital expenditures; and
- Specific information needs of management for decision making and asset control purposes.

<u>Betterments</u>

Where costs are incurred to improve an existing asset by increasing the service potential of that asset, decreasing operating costs, extending the useful life, or improving the quality of the output of that asset, the costs of the betterment will be capitalized, provided they are greater than the applicable capitalization threshold for that asset classification, otherwise they will be expensed.

Bulk Purchases

One time purchases of 'like' assets (can be separated into groups such as chairs, tables, desks, shelving, etc). Includes the acquisition and replacement of blocks of assets. Does not include replacement of individual assets as part of a normal maintenance program. Excludes computers, books and other items with a replacement cycle of less than five years.

If the value of each individual item is lower than the capitalization threshold and the total value of the bulk purchase (includes purchase cost, installation cost, transportation cost and costs to bring the item into service) is over $50,000, the purchase will be capitalized.

Capitalization Thresholds

Defined as the minimum value of an expenditure that meets the criteria of a tangible capital asset and that will be recorded as a tangible capital asset.

Asset Description	Threshold Amount
Land	--
Land Improvements	$ 7,500
Buildings	$ 50,000
Engineered Structures	$ 50,000
Machinery & Equipment	$ 7,500
Vehicles	$ 7,500
Betterments	$ 7,500
Bulk Purchases	$ 50,000

AMORTIZATION METHODS AND RATES

The cost of property, equipment and other tangible capital assets is essentially a long-term prepayment of an expense in advance of the use of the asset. As the economic service life of the asset expires, the cost of the asset is systematically allocated to operations as an expense called "amortization".

Periodic amortization expense should be an allocation of the historical cost of the asset less expected salvage (residual) value, if applicable, to operations in proportion to the economic benefits received each period from the use of the asset.

The service life of an asset should be measured in terms of years. Appendix A contains a complete list of recommended maximum useful lives for each class of assets that will be used for amortization purposes.

Straight-line amortization shall be generally used to calculate the annual charge to each department's accounts for the use of all tangible capital assets, except for certain machinery and equipment classifications, which shall be amortized based on number of hours of usage.

Amortization will be recorded on an annual basis. For example, where a type of asset has an average expected life of 3 years and the balance is $30,000, the annual straight line amortization would be calculated as 1/3 x $30,000, or $10,000. The amortization charges related to the asset should be reviewed for reasonableness at year-end.

Another important factor of Canadian tax law as it relates to amortization is the so called "half in the first year rule". According to this rule, in the first year of the ownership of an asset, the cost base used to determine the first year's amortization charge is half of the acquisition cost or recorded value. The County of Lethbridge **<u>will not</u>** be applying this rule for our amortization of assets.

The estimate of the useful life of the remaining unamortized portion of a tangible capital asset should be reviewed on a regular basis and revised when the appropriateness of a change can be clearly demonstrated.

REVIEWS AND WRITE-DOWNS

Decisions on the useful life and appropriate amortization method may change during the life of the asset and should be reviewed on a regular basis by each department.

When conditions indicate that a tangible capital asset no longer contributes to the government's 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, the cost of the tangible capital asset should be reduced to reflect the decline in the asset's value. Write-downs should not be reversed.

ASSET DISPOSAL

Disposals of assets may occur by sale, trade-in, destruction, loss or abandonment. Senior Management, Department Head, or other delegated staff are responsible for disposing of surplus assets. Legislative requirements (ie. Municipal Government Act) may be necessary to follow for disposal of certain assets.

Department Heads, or delegated staff, are responsible for informing the Finance Department by way of an Asset Disposal Form, any changes in asset inventory for accounting and insurance purposes (see Appendix B).

The difference between the net proceeds on disposal of a tangible capital asset and the net book value of the asset should be accounted for as a revenue or expense in the statement of operations.

REFERENCES

Canadian Institute of Chartered Accountants – Public Sector Accounting Standards, Section PS3150m, Tangible Capital Assets

Alberta Municipal Affairs and Housing (2007) Tangible Capital Assets Project – Implementation Toolkit

APPENDIX A: RECOMMENDED MAXIMUM USEFUL LIFE

ASSET CLASSES **Major** ***Minor*** **Sub-class One** ***Sub-class Two*** **Sub-class Three**	MAXIMUM USEFUL LIFE
Land	
Right-of-way	--
Undeveloped right-of-way	--
Parks	--
General	--
Cultural & Historical Assets	
Public art	--
Historical	--
Heritage site	--
Land Improvements	
Parking lot	
Gravel	15
Asphalt	25
Playground structures	15
Landscaping	25
Fences	20
Sprinkler systems	25
Fountains	20
Lakes/ponds	25
Retaining walls	20
Running tracks	15
Outdoor lighting	20
Airport runways	20
Runway/Approach Lighting	40
Bike/jogging Paths	
Gravel	15
Asphalt	20
Landfill	
Pits	Volume
Pads	Volume
Transfer stations	25
Construction in progress	--
Buildings	
Permanent Structures	
Architectural	Variable (15-25)
Structural – Frame, Metal, or Concrete	50
HVAC	Variable (15-50)
Roof	Variable (15-40)
Portable Structures	
Metal or Frame	25
Leasehold improvements	Variable (10-50)
Construction in progress	--

ASSET CLASSES **Major** ***Minor*** Sub-class One *Sub-class Two* Sub-class Three	MAXIMUM USEFUL LIFE
Engineered Structures	
Roadway system	
Bridges	
Steel culverts	**80**
Concrete culverts	**100**
Standard bridges	**60**
Major bridges	**100**
Curb & gutter	**30**
Roads & streets	
Lanes/alleys	
ACP - hot mix	**20***
Gravel	**15***
Nonconforming	**20***
Local/Collector/Arterial/Major Arterial	
Concrete	**30***
ACP - hot mix	**20***
ACP - cold mix	**10***
Chip seal	**10***
Oil	**5***
Gravel	**25***
Subsurface	**40***
Road signs	
Traffic control	**30**
Information	**30**
Lights	
Decorative	**30**
Street	**30**
Traffic	**30**
Guard rails	**30**
Ramps	**30**
Sidewalks & para-ramps	**30**
Construction in progress	**--** ** subject to weather conditions*
Water system	
Distribution system	
Mains	**75**
Services	**75**
Pump, lift and transfer stations	**45**
Plants and facilities	
Structures	**45**
Treatment equipment	
Mechanical	**45**
Electrical	**45**
General	**45**
Pumping equipment	**45**
Hydrants/fire protection	**75**
Reservoirs	**45**
Construction in progress	**--**

ASSET CLASSES **Major** ***Minor*** **Sub-class One** ***Sub-class Two*** **Sub-class Three**	MAXIMUM USEFUL LIFE
Wastewater system	
Collection system	
Mains	**75**
Services	**75**
Pump, lift and transfer stations	**45**
Plants and facilities	
Structures	**45**
Treatment equipment	
Mechanical	**45**
Electrical	**45**
General	**45**
Pumping equipment	**45**
Lagoons	**45**
Construction in progress	**--**
Storm system	
Collection system	
Mains	**75**
Services	**75**
Pump, lift and transfer stations	**45**
Catch basins	**75**
Outfalls	**75**
Wetlands	**75**
Retention ponds	**75**
Treatment facility	**45**
Construction in progress	**--**
Machinery and Equipment	
Heavy construction equipment	**Variable (5-25) (or # of hours)**
Stores	**25**
Food services	**10**
Fire equipment	**12**
Boats	**25**
Fitness and wellness	**10**
Control systems	**5**
Communication links	**20**
SCADA system	**10**
Fuelling stations	**15**
Laboratory	**10**
Communications	
Radios	**10**
Telephone systems	**10**
Tools, shop and garage equipment	**15**
Scales	**15**
Bins	**15**

ASSET CLASSES **Major** ***Minor*** **Sub-class One** ***Sub-class Two*** **Sub-class Three**	**MAXIMUM USEFUL LIFE**
Machinery and Equipment, *continued*	
Meters	
Electrical	**20**
Gas	**20**
Water	**40**
Office Furniture & Equipment	
Furniture	**20**
Office equipment	**10**
Audiovisual	**10**
Photocopiers	**5**
Computer Systems	
Hardware	**3-5**
Software	**10**
Construction in progress	**--**
Vehicles	
Light duty	**5-10**
Medium duty	**5-10**
Heavy duty	**5-10**
Fire trucks	
Engines (Type 1)	**20**
Water Tender (Tanker)	**20**
Rescue Unit (Rescue/Command)	**15**
Wildland Unit (Overland Rapid Response)	**15**
Command Unit	**10**
Construction in progress	**--**

APPENDIX B: ASSET DISPOSAL FORM

County of Lethbridge

Asset Disposal Form

Asset Description: ______________________________

Year/Make/Model: ______________________________

Fixed Asset # ______________ Serial # ______________

Check One:

Sold ☐ Donated ☐ Trade-In ☐ Other ☐

Disposal Date: ______________ Sale Price (if applicable): ______________
Do not include GST

Sold/Donated to: ______________________________

____

Department Head: ______________________ Date: ______________
Print Name

____
Signature

Comments: ______________________________

____

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Please forward completed and signed form with documentation supporting method of disposal and any monies received to Comptroller.