TANGIBLE CAPITAL ASSETS

Background

The Division will follow a prescribed procedure to record and manage the tangible capital assets (TCA) owned by the Division. The treatment of TCA for accounting purposes is intended to be in accordance with Generally Accepted Accounting Principles (G.A.A.P.), pronouncements of the Public Sector Accounting Board (P.S.A.B.) and the Province of Saskatchewan.

Purpose

This procedure will provide all departments with information for assessing their physical resources by providing framework for:

- establishing guidelines for activities relating to financing and administration of resources for acquisition, development or construction of TCA;
- ensuring that TCA are recorded appropriately and accurately;
- providing accountability over TCA; and
- gathering and maintaining information needed to prepare financial statements.

1. Scope

   This procedure applies to all Division departments, boards and councils, school based organizations and other organizations falling within the reporting entity of the Division.

2. Categorization of Assets

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

   2.1.1 Held for use in the production or supply of goods and services;
   2.1.2 Have useful lives extending beyond a fiscal year;
   2.1.3 Are intended to be used on a continuing basis; and,
   2.1.4 Are not intended for sale in the ordinary course of operations.

   TCA are a significant economic resource and key component in the delivery of programs and services. The benefits that are expected through the exercise of capitalizing TCA include:

   2.1.5 Maintain appropriate accountability for government-owned TCA;
   2.1.6 Ensure accounting consistency across the organization;
   2.1.7 Ensure efficient and effective use of assets; and
   2.1.8 Provide information that will support measuring the cost of the programs and services.

2.2 Elements of Cost

The cost of a tangible capital asset (*PSAB 3150.10)* is the gross amount of consideration given up to acquire, construct, develop or better a tangible capital asset and includes direct construction or development costs (such as materials and labour) and overhead costs directly attributable to the acquisition, construction or development of the asset. These costs may include but are not limited to:

- 2.2.1 Amount paid to vendors;
- 2.2.2 Transportation/freight charges to the point of initial use;
- 2.2.3 Handling and storage charges;
- 2.2.4 Direct design/production costs such as labour, equipment rentals, materials and supplies;
- 2.2.5 PST and other non-refundable taxes;
- 2.2.6 Engineering, architectural and other outside services for designs, plans, specifications and surveys;
- 2.2.7 Acquisition and preparation costs of buildings and other facilities;
- 2.2.8 Fixed equipment and related installation cost required for activities in a building or facility;
- 2.2.9 Direct costs of inspection, supervision and administration of construction contracts and work;
- 2.2.10 Legal and recording fees and damage claims;
- 2.2.11 Fair values of land, facilities and equipment donated;
- 2.2.12 Appraisal costs;
- 2.2.13 Advertising costs;
- 2.2.14 Application fees;
- 2.2.15 Supervisory fees;
- 2.2.16 Utility costs; and,
- 2.2.17 Site preparation costs

2.3 Primary Category

The primary asset category will be shown in the notes to the financial statements as "Segmented by Asset Class". The list of primary asset categories to be used is as follows:

- 2.3.1 Land
- 2.3.2 Land Improvements
- 2.3.3 Buildings
- 2.3.4 Equipment and Technology
- 2.3.5 Work in Progress

2.4 Functional Category

The functional asset category will be shown in the notes to the financial statements as "Segmented by Division". The list of functional asset categories follows the Ministry of Education return including, but not limited to:

- 2.4.1 Governance
- 2.4.2 Administration
- 2.4.3 Instruction
- 2.4.4 Plant Operation and Maintenance

2.4.5 Transportation
2.4.6 Complementary Services
2.4.7 External Services
2.4.8 Interest and Bank Charges

2.5 Excluded Assets

The following assets should not be capitalized and amortized:

2.5.1 Land (or other assets) acquired by right, such as Crown, forests, water and mineral resources;
2.5.2 Works of art and historical treasures; and
2.5.3 Intangible assets such as patents, copyrights, official plans, studies, trademarks.

2.6 Land

Land normally has an indefinite useful life that exceeds the useful lives of the buildings, roads or structures situated on the land. The cost of acquired land is separated from the other costs of an asset and maintained as a component. The cost of the acquired land is not amortized as land normally maintains its value over time.

2.7 Equipment and Technology

2.7.1 Equipment includes fixed or moveable TCA to be used for operations, the benefits of which extend beyond one year from date of receipt and are above the threshold level.

2.7.2 Technology includes computers and consists of hardware and software (purchased and created) that can be considered a component of, is typically attached to, or communicates with an information system.

2.8 Work In Progress

2.8.1 Work in Progress is the construction or development of a capital asset that extends over several years.

2.8.2 Work in progress is not capitalized or amortized until the asset is in use. The capital costs for such an asset should be accumulated until the asset is ready for use.

2.8.3 A work in progress account should be established to allow capital costs to be tracked separately for easy identification in reporting.

2.8.4 Amortization is calculated and begins the first fiscal year that the asset is in use.

2.9 Contributed Assets

2.9.1 A tangible capital asset may be gifted or contributed (*PSAB 3150.14*) by an external third party with no cash outlay.

2.9.2 Where an asset is acquired through a third party contribution, the amount to record the asset at is the cost provided by the contributor. If the cost cannot be provided, a fair value may be estimated using either market or appraised values or a qualified third party evaluation. When an estimate of fair value cannot be reasonably estimated, the asset will be recognized at a nominal value.

2.10 Acquired, Constructed or Developed Assets

2.10.1 Cost includes all cost directly attributable (i.e. construction, architectural and other professional fees) to the acquisition, construction or development of the asset. Carrying costs such as internal design, inspection, administrative and other similar costs may be capitalized. Capitalization of general administrative overheads is not allowed.

2.11 Heritage Assets

2.11.1 Heritage assets *(PSAB 3150.08)* are works of art and historical treasures considered irreplaceable and preserved in trust for future generations. Collections or individual items of significance that are owned and not held for financial gain but rather public exhibition, education or research in maintenance of public service may be considered heritage assets. Heritage assets will not be recognized as TCA in financial statements, but the existence of such property should be disclosed *(PSAB 3150.42(e))*.

2.11.2 Amortization of heritage assets does not apply as the economic benefit or service potential of heritage assets are used up so slowly and the estimated useful lives are extraordinarily long.

2.12 Capital Leases

2.12.1 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. If the arrangement is an operating lease, not all benefits and risks transferred to lessee, then the lease payments should be expensed and no liability is recorded. Capital leases are recorded as if the lessee had acquired the asset and assumed liability.

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

2.12.2.1 There is reasonable assurance that the division will obtain ownership at the end of the lease;

2.12.2.2 The division will receive substantially all of the economic benefits of the assets;

2.12.2.3 The leaser is assured of recovering the investment in the asset and earning a return.

2.12.2.4 Where at least one of the conditions in the preceding paragraph is not present, other factors may indicate that a capital lease exists. For example:

- The division owns or retains control of the land on which a leased asset is located and the asset cannot be easily moved;
- The division contributes significant assistance to finance the cost of acquiring or constructing the asset that it will lease or
- The division bears other potential risks, such as obsolescence, environmental liability, uninsured damage or condemnation of the asset and any of these are significant.

2.12.3 If the thresholds are met, a capital asset and a liability should each be recorded for the present value of the minimum lease payments. The leased asset should be amortized over the lesser of the lease term or the estimated useful life for similar capital assets outlined in Schedule A. Maintenance costs should be excluded when calculating minimum lease payments. The discount rate should be the lesser of the division's incremental borrowing rate or the interest rate implicit in the lease, if determinable.

3. Capitalization Threshold

3.1 Capitalization threshold relates to the minimum dollar threshold that is used to assist in determining which expenditures will be capitalized as assets and amortized and which expenditures will be treated as current year expenses. The capitalization threshold has an impact on the size of the asset inventory and the complexity of managing subsequent acquisitions and disposals.

3.1.1 The capitalization threshold levels established and presented in schedule A are a balance between the accurate presentation of information for decision-making and the cost of acquiring and maintaining such information.

3.1.2 Where it is not practical and cost effective to establish a reasonable estimate of historical cost, departments may use appraised or some appropriate measure of current value and extrapolate back to estimated historical cost using relevant price/cost index *(PSAB 3150.47)*.

3.1.3 Where historical records cannot be located in order to value an asset, it is necessary to develop costs in today's dollars and then discount them back to the date the asset was constructed/acquired.

3.1.4 Where the year the asset was constructed or acquired is unknown, an estimate for the number of years remaining and the current value of the asset, working backward in order for an estimated year and value can be determined.

3.2 Pooled Assets

3.2.1 Departments must be aware of the impact that pooling of assets might have. For example, when the value of an individual item is less than the threshold level, but upon acquiring several of these assets in a single purchase or when these costs are aggregated, the asset makes up a significant group that exceeds the threshold level then they must be capitalized.

3.2.2 Assets to be pooled are designated below and shall be reviewed with the Chief Financial Officer on an annual basis.
- 3.2.2.1 Computers
- 3.2.2.2 Furniture and Equipment
- 3.2.2.3 Vehicles
- 3.2.2.4 Leased Capital Assets

3.3 Useful Life

3.3.1 Useful life *(PSAB 3150.28)* is the estimate of the period over which tangible capital asset is used and is established in schedule B. The economic or physical life of an asset may be extended beyond the useful life of an asset. Estimating useful lives of assets is a matter of judgment based on experience and should be applied on a consistent basis. Factors to be considered in estimating the useful life include:
- 3.3.1.1 Expected future usage;
- 3.3.1.2 Technical obsolescence;
- 3.3.1.3 Expected wear and tear through the passage of time;
- 3.3.1.4 Maintenance program; and
- 3.3.1.5 Condition of existing comparable items.

3.3.2 The service potential of an asset is normally consumed through usage. Factors such as obsolescence, excessive wear and tear or other events could significantly diminish the service potential that was originally anticipated from the asset. The estimated useful life of an asset category and remaining useful life of individual assets should be reviewed by the Manager, in conjunction with the Chief Financial Officer on a regular basis and revised when appropriate. The rationale supporting the decision to revise useful life estimates of an asset should be documented.

3.3.3 Significant events that may indicate a need to revise the estimated useful life of an asset may include:
- 3.3.3.1 Completion of a major betterment;
- 3.3.3.2 Change in extent that the asset is used;
- 3.3.3.3 Change in the manner that the asset is used;
- 3.3.3.4 Removal of asset from service for extended period of time;
- 3.3.3.5 Physical damage or destruction;
- 3.3.3.6 Significant technological developments; and,
- 3.3.3.7 Change in law, environment or public preferences that affect usage and time periods over which asset are used.

3.3.4 A number of factors may trigger the need for a review of the expected useful life of an asset or its components such as major investments including upgrades to critical components:

3.3.4.1 Significant changes in the market value;

3.3.4.2 Pattern of differences in rate of wear and tear compared to that previously expected;

3.3.4.3 Pattern of differences in levels of maintenance compared to that previously expected;

3.3.4.4 Results from engineering testing indicating higher than expected rates of structural deterioration;

3.3.4.5 Major changes in technology increasing the rates of obsolescence for critical components;

3.3.4.6 Major changes in government programs impacting the expected use of assets;

3.3.4.7 Major changes in government regulations, policies or standards impacting expected use of assets; and

3.3.4.8 Major damage to an asset.

4 Betterments

4.1 Betterment

4.1.1 Betterment *(PSAB 3150.19)* are considered to be capital asset additions for the assets to which they relate and should be recorded as part of the main asset but need to have their own identification number and tracked separately. Betterments which meet the threshold of the applicable capital asset category are capitalized; under the threshold they are expensed.

4.1.2 Betterments are enhancements to the service potential of a capital asset, such as:

4.1.2.1 A reduction in associated operating costs;

4.1.2.2 An extension of useful life, by more than 25%; and,

4.1.2.3 An improvement in the quality of output by more than 10%.

4.1.3 Where a betterment enhances the service potential of a capital asset without increasing its estimated useful life, the amortization period should remain the same. If however, the betterment increases the estimated useful life of a capital asset, its useful life for amortization should also change.

4.2 Repairs and Maintenance

4.2.1 Repairs and maintenance *(PSAB 3150.21(a))* expenditures are costs to keep the condition of an asset at its expected operating standard. These expenditures are usually incurred on a more or less continuous basis. For example, regular maintenance activities prescribed by the manufacture of a new heating, ventilation and air conditioning system (HVAC) would normally be required to ensure that the asset is able to provide service at a level and quality as originally intended by the manufacturer. Performance of regular maintenance may also be required as part of the product warranty provided by the manufacturer. The costs of regular

maintenance will be expensed. Costs that do not increase the original assessed useful life, service capacity or quality of output would be expenses as incurred. They include:

4.2.1.1 Repairs to restore assets damaged by fire, flood, accidents 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; and

4.2.1.2 Routine maintenance and expenditures, such as repainting, cleaning and replacing minor parts.

4.3 Replacement

4.3.1 Replacements involve the removal of component parts and substitution of a new part or component of essentially the same type and performance capabilities. If the component being replaced had been previously segregated in the accounting records as a distinct asset for amortization over a specific expected useful life and meets the threshold of the applicable asset class, the new component is capitalized and the old component is retired with its residual net book value removed from the accounts. The original cost of the old component and the related accumulated amortization should be removed from the accounting records.

4.3.2 If the component being replaced was not significant enough to be previously segregated from the whole property as a distinct asset, then the replacement is normally considered a repair and the costs are expensed as incurred. If the replacement of the component results in an enhancement of the service potential of the property as a whole, the replacement is considered betterment and the costs are capitalized.

4.4 Additions

4.4.1 Additions are made to an existing asset to extend, enlarge or expand the existing asset. As additions increase service capacity or physical output of a property, they are betterments. The costs of additions should be capitalized.

4.5 Upgrades

4.5.1 Upgrades involve the removal of a major part or component of an asset and the substitution of a different component having significantly improved performance capabilities beyond the property's original design standard. Refer to "Disposal" section for financial implications.

4.5.2 An upgrade increases the overall efficiency (i.e. increasing utilization, lowering operating costs, or increasing output of service) quality or extends the expected useful life of an asset. The costs of upgrades are capitalized.

4.5.3 The following examples would have characteristics of an upgrade:

4.5.3.1 Installing air conditioning in a building that was previously not air-conditioned increasing the service quality of the property;

4.5.3.2 Replacing existing lighting with energy saving lighting reducing future operating costs;

4.5.3.3 Substituting a tile roof for wooden shingle increasing the expected useful life of the building beyond its current estimated useful life; or

4.5.3.4 Replacing a furnace with a high efficiency furnace decreasing future operating costs.

4.6 Adjustments

4.6.1 Trade-in

4.6.1.1 A trade in occurs when an asset is disposed and replaced with a new asset through the same supplier in the same transaction. This transaction should be accounted for as two separate entries. The trade in value should be treated as proceeds of disposal and is used in calculating the gain or loss on the disposal of the asset being traded in. 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.

4.6.2 Disposal

4.6.2.1 The disposal of a capital asset results in its removal from service as a result of sale, destruction, loss or abandonment. When a capital asset is disposed of, the cost and the accumulated amortization should be removed from the accounting records and any gain or loss is recorded at that time. Costs that are associated with the disposal and paid by the Division should be expensed.

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

4.6.4 Write Down/Off

4.6.4.1 A capital asset should be written down when a reduction in the value of the asset's service potential can be measured and the reduction is expected to be permanent.

4.6.4.2 Write downs of capital assets should be accounted for as an expense in the current period.

4.6.4.3 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.

4.6.4.4 Conditions that indicate a write down is necessary may include a change in manner or extent to which the asset is used:

4.6.4.4.1 Removal of the asset from service;

5.1.1.1.1 Physical damage;
5.1.1.1.2 Significant technological developments;
5.1.1.1.3 A decline in, or cessation of the need for the service provided by the asset; or
5.1.1.1.4 A change in the law or environment affecting the extent to which the asset can be used.

5 Amortization

5.1 Amortization is the allocation of the cost of an asset less its estimated residual value to expense over the estimated useful life of the asset *(PSAB 3150.22)*. The asset will be used to provide services or deliver programs to the public over the assets' estimated useful lives.

5.2 Where the residual value of the asset is significant then it should be factored into the calculation of amortization otherwise assume a zero residual value for the components.

5.3 Amortization should be recognized in a rational and systematic basis appropriate to the nature and use of the asset. Amortization should reflect as closely as possible to the extent to which an asset's service potential is consumed over its useful life.

5.4 Amortization should start as soon as an asset is completed and ready for use. This would be the case even if the decision were made to delay placing the asset into service.

5.5 Where construction of an asset is comprised of distinct, multiple and self-contained phases, amortization must begin for the distinct phases that are completed.

5.6 Amortization will be calculated on a full year basis.

5.6.1 A full year's amortization is recorded in the year the asset is acquired, constructed or developed and put into use, regardless of when this event occurs in the fiscal year.

5.7 Amortization is calculated using the **straight-line method** based on the estimated useful life of each asset.

5.7.1 The straight-line method is calculated by dividing the asset's original cost, less estimated residual value, by its estimated life in years. This yields a constant annual amortization amount each year. For example, a building that costs $3,000,000 has an estimated useful life of 40 years would yield annual amortization of $75,000 ($3,000,000/40 years. Land has an unlimited useful life and should not be amortized.

6 Appendices

6.1 Appendix A – Categorization of Assets

6.2 Appendix B – Thresholds and Useful Lives

6.3 Appendix C – Definitions

6.4 Appendix D – Capitalization Methods for Historical Costs

Reference: Section 87, 109, 110 Education Act

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