Public Sector Accounting Handbook
Section 3150 - Tangible Capital Assets

Section PS 3150
Tangible Capital Assets

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PURPOSE AND SCOPE

.01 This Section establishes standards on how to account for and report tangible capital assets in government financial statements. 1

.02 Tangible capital assets are a significant economic resource managed by governments and a key component in the delivery of many government programs. Tangible capital assets include such diverse items as roads, buildings, vehicles, equipment, land, water and other utility systems, aircraft, computer hardware and software, dams, canals, and bridges.

.03 This Section does not apply to intangible assets, natural resources, and Crown lands that have not been purchased by the government.

.04 Government capital grants and government transfers of tangible capital assets would be accounted for in accordance with GOVERNMENT TRANSFERS, Section PS 3410.

DEFINITIONS

.05 For the purposes of this Section:

(a) **Tangible capital assets** are non-financial assets 2 having physical substance that:

(i) 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;

(ii) have useful economic lives extending beyond an accounting period;

(iii) are to be used on a continuing basis; and

(iv) are not for sale in the ordinary course of operations.

(b) **Cost** is 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 cost of a leased tangible capital asset is determined in accordance with PUBLIC SECTOR GUIDELINE PSG-2, Leased Tangible Capital Assets.

(c) **Fair value** is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

(d) **Net book value** of a tangible capital asset is its cost, less both accumulated amortization and the amount of any write-downs.

(e) **Residual value** is the estimated net realizable value of a tangible capital asset at the end of its useful life to a government.

(f) **Service potential** is 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.

(g) **Useful life** is 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.

ACCOUNTING

.06 Governments need to present information about the complete stock of their tangible capital assets and amortization in the summary financial statements to demonstrate stewardship and the cost of using those assets to deliver programs and provide services.

.07 ♦ *Tangible capital assets should be accounted for and reported as assets on the statement of financial position.* [APRIL 2005]

.08 Works of art and historical treasures are property that has cultural, aesthetic or historical value that is worth preserving perpetually. Works of art and historical treasures would not be recognized as tangible capital assets in government financial statements because a reasonable estimate of the future benefits associated with such property cannot be made. Nevertheless, the existence of such property should be disclosed (see paragraph PS 3150.42(e)).

Measurement

Cost

.09 ♦ *Tangible capital assets should be recorded at cost.* [SEPT. 1997]

.10 The cost of a tangible capital asset includes the purchase price of the asset 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. The activities necessary to prepare a tangible capital asset for its intended use encompass more than the physical construction of the tangible capital asset. They include the technical and administrative work prior to the commencement of and during construction.

.11 The cost of each tangible capital asset acquired as part of a single purchase (for example, the purchase of a building and land for a single amount) is determined by allocating the total price paid for all of the tangible capital assets acquired to each one on the basis of its relative fair value at the time of acquisition.

.12 Many tangible capital assets, particularly complex network systems such as those for water and sewage treatment, consist of a number of components. Whether a government decides to record and account for each component as a separate asset will be determined by the usefulness of the resulting information to the government and the cost versus the benefit of collecting and maintaining it.

.13 When, at the time of acquisition, a portion of the acquired tangible capital asset is not intended for use, its costs and any costs of disposal, net of any estimated proceeds, are attributed to that portion of the acquired tangible capital asset that is intended for use. For example, the cost of acquired land that includes a building that will be demolished includes the cost of the acquired property and the cost of demolishing the building.

.14 Governments may receive contributions of tangible capital assets. The cost of a contributed asset is considered equal to its fair value at the date of contribution. Fair value of a contributed tangible capital asset may be estimated using market or appraisal values. In unusual circumstances, where an estimate of fair value cannot be made, the tangible capital asset would be recognized at nominal value.

.15 The cost of a tangible capital asset that is acquired, constructed or developed over time includes carrying costs directly attributable to the acquisition, construction or development activity, such as interest costs when the government's policy is to capitalize interest costs.

.16 Carrying costs incurred while land acquired for building purposes is held without any associated construction or development activity do not qualify for capitalization.

.17 Capitalization of carrying costs ceases when no construction or development is taking place or when a tangible capital asset is ready for use in producing goods or services. A tangible capital asset is normally ready for productive use when the acquisition, construction or development is substantially complete.

.18 Determining when a tangible capital asset, or a portion thereof, is ready for productive use requires consideration of the circumstances in which it is to be operated. Normally it would be predetermined by a government by reference to factors such as productive capacity, occupancy level, or the passage of time.

.19 Costs of betterments are considered to be part of the cost of a tangible capital asset and would be added to the recorded cost of the related asset. A betterment is a cost incurred to enhance the service potential of a tangible capital asset. In general, for tangible capital assets other than complex network systems, 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.

.20 This definition of a betterment is more difficult to apply to tangible capital assets that are complex network systems and are very long-lived, such as highway and water systems, because identifying expenditures that would extend their lives may not be practicable. For example, expenditures on road systems to widen the roads or add to the number of lanes expand the capacity of the road system to provide services and are clearly betterments. On the other hand, expenditures incurred to maintain the originally anticipated service potential of a road, or its estimated useful life, are more in the nature of maintenance.

.21 For complex network systems, therefore, the following basic distinctions can be used to identify maintenance and betterments:

(a) Maintenance and repairs 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.

(b) Betterments increase service potential (and may or may not increase the remaining useful life of the tangible capital asset). Such expenditures would be included in the cost of the related asset.

Amortization

.22 ♦ *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.* [SEPT. 1997]

.23 ♦ *The amortization of the costs of tangible capital assets should be accounted for as expenses in the statement of operations.* [SEPT. 1997 *]

.24 Land normally has an unlimited life and would not be amortized.

.25 Most tangible capital assets, however, have limited useful lives. This fact is recognized by amortizing the cost of tangible capital assets in a rational and systematic manner over their useful lives. Amortization expense is an important part of the cost associated with providing government services, regardless of how the acquisition of tangible capital assets is funded. Information about a program or activity's total costs is relevant to any assessment of the benefits the program or activity provides.

.26 Different methods of amortizing a tangible capital asset result in different patterns of cost recognition. The objective is to provide a systematic and rational basis for allocating the cost of a tangible capital asset, less any residual value, over its useful life. A straight-line method reflects a constant charge for the service as a function of time. A variable charge method reflects service as a function of usage. Other methods may be appropriate in certain situations.

.27 Where a government expects the residual value of a tangible capital asset to be significant, it would be factored into the calculation of amortization.

.28 The useful life of a tangible capital asset depends on its expected use by the government. Factors to be considered in estimating the useful life of a tangible capital asset include:

(a) expected future usage;

(b) effects of technological obsolescence;

(c) expected wear and tear from use or the passage of time;

(d) the maintenance program;

(e) studies of similar items retired; and

(f) the condition of existing comparable items.

.29 ♦ *The amortization method and 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.* [SEPT. 1997]

.30 Significant events that may indicate a need to revise the amortization method or the estimate of the remaining useful life of a tangible capital asset include:

(a) a change in the extent to which the tangible capital asset is used;

(b) a change in the manner in which the tangible capital asset is used;

(c) removal of the tangible capital asset from service for an extended period of time;

(d) physical damage;

(e) significant technological developments;

(f) a change in the demand for the services provided through use of the tangible capital asset; and

(g) a change in the law or environment affecting the period of time over which the tangible capital asset can be used.

Write-downs

.31 ♦ *When conditions indicate that a tangible capital asset no longer contributes to a 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.* [SEPT. 1997]

.32 ♦ *The net write-downs of tangible capital assets should be accounted for as expenses in the statement of operations.* [SEPT. 1997 *]

.33 ♦ *A write-down should not be reversed.* [SEPT. 1997]

.34 A government would write down the cost of a tangible capital asset when it can demonstrate that the reduction in future economic benefits is expected to be permanent. Conditions that may indicate that the future economic benefits associated with a tangible capital asset have been reduced and a write-down is appropriate include:

(a) a change in the extent to which the tangible capital asset is used;

(b) a change in the manner in which the tangible capital asset is used;

(c) significant technological developments;

(d) physical damage;

(e) removal of the tangible capital asset from service;

(f) a decline in, or cessation of, the need for the services provided by the tangible capital asset;

(g) a decision to halt construction of the tangible capital asset before it is complete or in usable or saleable condition; and

(h) a change in the law or environment affecting the extent to which the tangible capital asset can be used.

.35 The persistence of such conditions over several successive years increases the probability that a write-down is required unless there is persuasive evidence to the contrary.

.36 When the tangible capital asset no longer contributes to the government's ability to provide goods and services, it would be written down to residual value, if any. This would be appropriate when the government has no intention of continuing to use the asset in its current capacity, and there is no alternative use for the asset.

.37 In other circumstances, it will be necessary to estimate the value of expected remaining future economic benefits. Where a government can objectively estimate a reduction in the value of the asset's service potential to the government, and has persuasive evidence that the reduction is expected to be permanent in nature, the tangible capital asset would be written down to the revised estimate of the value of the asset's remaining service potential to the government.

Disposals

.38 ♦ *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.* [SEPT. 1997 *]

.39 Disposals of government tangible capital assets in the accounting period may occur by sale, destruction, loss or abandonment. Such disposals represent a reduction in a government's investment in tangible capital assets, regardless of how that investment is reported.

PRESENTATION AND DISCLOSURE

.40 ♦ *The financial statements should disclose, for each major category of tangible capital assets and in total:*

(a) *cost at the beginning and end of the period;*

(b) *additions in the period;*

(c) *disposals in the period;*

(d) *the amount of any write-downs in the period;*

(e) *the amount of amortization of the costs of tangible capital assets for the period;*

(f) *accumulated amortization at the beginning and end of the period; and*

(g) *net carrying amount at the beginning and end of the period.* [APRIL 2005]

.41 Major categories of tangible capital assets would be determined by type of asset, such as land, buildings, equipment, roads, water and other utility systems, and bridges.

.42 ♦ *Financial statements should also disclose the following information about tangible capital assets:*

(a) *the amortization method used, including the amortization period or rate for each major category of tangible capital asset;*

(b) *the net book value of tangible capital assets not being amortized because they are under construction or development or have been removed from service;*

(c) *the nature and amount of contributed tangible capital assets received in the period and recognized in the financial statements;*

(d) *the nature and use of tangible capital assets recognized at nominal value;*

(e) *the nature of the works of art and historical treasures held by the government; and*

(f) *the amount of interest capitalized in the period.* [SEPT. 1997]

TRANSITIONAL PROVISIONS FOR LOCAL GOVERNMENTS

.43 This Section applies to local governments for fiscal years beginning on or after January 1, 2009. Earlier adoption is encouraged.

.44 This Section applies to all tangible capital assets.

.45 When, during the period of transition, a local government has information on some but not all categories of its tangible capital assets, the local government would disclose information in accordance with PUBLIC SECTOR GUIDELINE PSG-7, Tangible Capital Assets of Local Governments.

.46 All government tangible capital assets would be recorded in a government's accounting system according to this Section. The information recorded would include the actual or estimated original cost of the tangible capital assets, their estimated useful lives and the related estimated accumulated amortization. When recording the initial value of a tangible capital asset for the purposes of applying this Section, consideration would be given to whether the net book value of the tangible capital asset is in excess of the future economic benefits expected from its use and, therefore, whether a write-down is required to establish more appropriate cost and accumulated amortization amounts for the asset.

.47 When a government does not have historical cost accounting records for its tangible capital assets, it will need to use other methods to estimate the cost and accumulated amortization of the assets. It may be possible to derive information for recording tangible capital assets from records of government departments that manage those assets. A government would apply a consistent method of estimating the cost of the tangible capital assets for which it does not have historical cost records, except in circumstances where it can be demonstrated that a different method would provide a more accurate estimate of the cost of a particular type of tangible capital asset.

.48 Some government tangible capital assets that are still in use by the government may not have any unamortized cost remaining because of their age and the amortization period set for that type of tangible capital asset. A record of such tangible capital assets would, however, need to be set up for asset control purposes. If a government has the information to estimate the historical cost and accumulated amortization of such fully amortized assets, then that information would be recorded in the accounting records. If a local government does not have this detailed information on its fully amortized assets, it would disclose them at an initial value equal to their residual value, where material and previously known. Otherwise it would disclose them at a nominal value.

Footnotes

1. The term "financial statements" refers to the summary financial statements prepared by a government to report on its financial condition and results of operations.

2. For the purposes of this Section, tangible capital assets are defined to include computer software.

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