

MUNICIPALITY OF CENTRAL MANITOULIN

BY-LAW 2009-02

BEING a By-law to approve a Policy to Prescribe the Accounting Treatment for Tangible Capital Assets

WHEREAS the Public Sector Accounting Board (PSAB) has approved the reporting of all tangible capital assets for municipalities, beginning January 1st 2009;

AND WHEREAS Councils are required to pass a policy to deal with the treatment for tangible capital assets;

AND WHEREAS the Canadian Institute of Chartered Accountants, (CICA) has developed guidelines to assist municipalities in the creation of a policy.

NOW THEREFORE the Council of the Municipality of Central Manitoulin enacts as follows:

1. That Schedule "A" attached hereto shall be approved as the policy prescribed for the accounting treatment for tangible capital assets of the Municipality of Central Manitoulin.
2. That this by-law shall come into force and take effect immediately up passing.

READ A FIRST AND SECOND TIME THIS 8th DAY OF JANUARY 2009.

READ A THIRD TIME AND FINALLY ENACTED IN OPEN COUNCIL THIS 8th DAY OF JANUARY 2009.

Reeve – Richard Stephens

Clerk – Ruth Frawley

I, _____, Clerk of the Municipality of Central Manitoulin, hereby certify that the following is a true copy of By-Law Number 2009-02 passed by the Municipality of Central Manitoulin on _____, 2009.

Clerk

Municipality Of Central Manitoulin
Tangible Capital Asset Policies 2009

The Municipality of Central Manitoulin will follow a prescribed administrative policy to record and manage the tangible capital assets owned by Central Manitoulin. The treatment of tangible capital assets 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 requirements of the Province of Ontario.

PURPOSE:

This policy will provide departments with information for assessing their stewardship of physical resources by providing a framework for:

- Establishing guidelines for activities relating to program planning, financing and administration of resources for the acquisition, development or construction of tangible capital assets;
- Maintaining manageable levels of long-term debt and facilitating the movement toward Council directed pay-as-you-go capital financing;
- Maximizing the use of internal sources of funding from current budget funding (capital levy and capital reserves);
- Ensuring that tangible capital assets are recorded appropriately and accurately due to their role in the delivery of local programs and services;
- Using value-added information that will impact decisions such as allocation and use of financial resources, assessment of financial condition, performance measurement, comparison with budgets, compliance with legislation, management of risks and management of assets. The information will be relevant and reliable by being timely, consistent, unbiased, clearly presented and readily understandable.

ACCOUNTABILITY

Council:

- Accountable to the public for approving acquisition, control and disposal of tangible capital assets;
- Accountable to the public for approving policies, procedures and guidelines as they relate to the management and financing of tangible capital assets.

Chief Administrative Officer:

- Accountable for development of processes to reflect corporate priorities;
- Accountable for development of tangible capital asset plan for Council that will provide long-term sustainability of services.

Treasurer:

- Accountable to prepare the tangible capital asset program;
- Accountable to have detailed knowledge of capital program submission;
- Accountable for effective use of available resources to manage the capital program;
- Accountable to ensure that implementation of recommendations are reflected in reports to Council;
- Identify controlled assets with values below the materiality threshold for a particular asset classification and a useful life in excess of one year;
- Differentiate between betterment and maintenance expenditures;
- Ensure timely completion of capital projects and transfer of assets from work in progress to tangible capital assets.

ADMINISTRATION

Tangible Capital Assets (Definition)

Tangible capital assets are non-financial assets with physical substance that are acquired, constructed or developed and:

- Held for use in the production or supply of goods and services;
- Have useful lives extending beyond an accounting period (normally 1 year);
- Are intended to be used on a continuing basis; and
- Are not intended for sale in the ordinary course of operations.

Tangible capital assets are a significant economic resource and a key component in the delivery of programs and services. The benefits from capitalizing tangible capital assets include:

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

Elements of Cost

The cost of a tangible capital asset is the gross amount of consideration given 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 attributed to the acquisition, construction or development of the asset. These costs may include but are not limited to:

- Amounts paid to vendors;
- Transportation/freight charges to the point of initial use;
- Handling and storage charges;
- Direct design/production costs such as labour, equipment rentals, materials and supplies;
- Engineering, architectural and other outside services for designs, plans, specifications and surveys;
- Acquisition and preparation costs of buildings and other facilities;
- Fixed equipment and related installation costs required for activities in a building or facility;
- Direct costs of inspection, supervision and administration of construction contracts and work;
- Legal and recording fees and damage claims;
- Fair values of land, facilities and equipment donated;
- Appraisal costs;
- Advertising costs;
- Application fees;
- Supervisory fees;
- Utility costs;
- Site preparation costs;
- Transportation insurance costs; customs and duty charges;
- Interest charges during acquisition, construction or development (up to substantial completion of 90%) or in the case of major projects (up to the issuance of the certificate of substantial completion).

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.

Furniture, Equipment and Technology

Furniture and equipment includes fixed or moveable tangible capital assets to be used for operations, the benefits of which extend beyond one year from date of receipt. Technology includes computers and consists of hardware and software (canned and customized) that can be considered a component of, is typically attached to, or communicates with an information system. The term encompasses processing units, memory apparatus, input and output devices, storage devices, connectivity equipment, printers and copiers.

Furniture, equipment and technology (FE&T) may be capitalized as pooled assets in the following situations:

- Construction of a new building;
- Construction of a new building which is a replacement for a currently existing building;
- Construction of a building addition that includes new FE&T;
- Major renovation of a building in which new FE&T is included to replace the existing items;
- Construction of certain major complex network systems (i.e. telephone, computers, servers, printers).

Work/Construction In Progress

Work or construction in progress represents the costs incurred to date on a project in which Central Manitoulin has not yet completed. Examples might include road, water and sewer infrastructure or

custom-developed computer software systems that have not reached substantial completion (i.e. 90%) or the asset has not been placed into production/service/use.

Work in progress for assets under development or construction must be recorded on the financial statements for the accounting period. All costs associated with these assets that are in the construction phase are to be capitalized. Work in progress is *not amortized*. Work in progress balances must be reconciled and the appropriate transfers from work in progress made to completed assets or written off to ensure that only active and incomplete work in progress is carried forward to the next period. The reconciliation should be done quarterly or at a minimum must be done annually.

For major projects, work in progress should be transferred to a tangible capital asset once the architect, engineer or consultant has issued the certificate of substantial completion or for other projects Central Manitoulin has issued the certificate of initial acceptance. Either certificate will provide evidence that the asset has met engineering and safety standards and is ready to be placed into production/service or occupied.

Contributed Assets

A tangible capital asset may be gifted or contributed by an external third party with no cash outlay. For example, land may be contributed by another level of government at zero or nominal consideration to facilitate the construction of a roadway or structure. A developer may install services such as water/sewer mains or roads within a subdivision at its own cost and then turn them over to the municipality to operate, maintain and replace. Where an asset is acquired at no cost or for nominal value, the amount recognized should be equal to its fair value as at the acquisition date. Fair value may be estimated using market or appraised values. When an estimate of fair value cannot be reasonably estimated, the asset will be recognized at its nominal value.

Heritage Assets

Heritage assets are works of art and historical treasures considered irreplaceable and preserved in trust for future generations. Collections or individual items of significance (i.e. carved wooden bowl, paintings, sculptures, structures) that are owned by Central Manitoulin and not held for financial gain but rather for public exhibition, education or research in furtherance of public service may be considered heritage assets.

Heritage assets will not be recognized as tangible capital assets in financial statements, but the existence of such property should be disclosed. 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. Due to the cultural, aesthetic or historical value, Central Manitoulin applies efforts to protect and preserve the asset indefinitely.

Accounting

All tangible capital assets and amortization must be identified and valued using an appropriate cost base; namely, historical cost. 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 historical cost, departments may use appraised or some appropriate measure of current value and extrapolate back to estimate historical cost using relevant price/cost index. Replacement cost should not be used unless it is the lower of cost alternatives. Tangible capital asset classifications that were historically established on whole asset or pooled asset approaches may be recorded using a component approach on a "go-forward" basis.

Capitalization Threshold

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.

Different categories of municipal assets will hold their own capital thresholds. Departments may recognize that it might be important to track and inventory items for management purposes but not necessarily capitalize and amortize those assets. There may also be exceptions to the application of

a threshold level. For example, a personal computer may be below the threshold level but when several computers are acquired then the bulk purchase would warrant treatment as a capital asset. See Appendices on Page 8 for specific capital thresholds for Central Manitoulin's asset categories.

Pooled Assets

Departments must be aware of the impact that pooling of assets (i.e. furniture, water/sewer service laterals, valves, landfill containers or road resurfacing) 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.

USEFUL LIFE

Useful life is the estimate of the period over which a tangible capital asset is used. The economic or physical life of an asset may extend beyond the useful life of an asset. Depending on the nature of the asset, useful life may be expressed in terms of time (years or machine hours) or output (production or service units). Estimating useful lives of assets is a matter of judgement based on experience and should be applied on a consistent basis. Factors to be considered in estimating the useful life include:

- Expected future usage;
- Technical obsolescence;
- Expected wear and tear through the passage of time;
- Maintenance program; and
- Condition of existing comparable items.

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 on a regular basis and revised when appropriate. The rationale supporting the decision to revise useful life estimates of an asset should be documented. Significant events that may indicate a need to revise the estimated useful life of an asset may include:

- Completion of a major betterment;
- Change in extent that the asset is used;
- Change in manner that the asset is used;
- Removal of asset from service for extended period of time;
- Physical damage or destruction;
- Significant technological developments;
- Change in law, environment or public preferences that affect usage and time periods over which asset is used.

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:

- Significant changes in the market value;
- Pattern of differences in rate of wear and tear compared to that previously expected;
- Pattern of differences in levels of maintenance compared to that previously expected;
- Results from engineering testing indicating higher than expected rates of structural deterioration;
- Major changes in technology increasing the rates of obsolescence for critical components;
- Major changes in government programs impacting the expected use of assets;
- Major changes in government regulations, policies or standards impacting expected use of assets;
- Major damage to an asset.

Differentiation (Betterment and Maintenance)

Betterments

Betterments are considered to be capital asset additions for the assets to which they relate and should be recorded as a sub category to the main asset. The cost should be recorded as a capital repair and maintenance expense within that year.

Maintenance

Maintenance 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 manufacturer 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 (i.e. lubrication of motor and compressors, replacement of filters). Performance of regular maintenance may also be required as part of the product warranty provided by the manufacturer. Costs that do not increase the original assessed useful life, service capacity or quality of output would be expensed as incurred.

Types of Betterment

Replacement

Replacements involve 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 its specific expected useful life, then the new component is capitalized and the old component is retired with its residual net book value removed from the accounts. If on the other hand, 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. Enhancements to service potential only result from replacements which extend the useful life of the property as a whole, increase the capacity or usage of the property, improve the quality of the property to a higher building class or improve the overall operating efficiency of the property.

Additions

Additions are made to an existing asset to extend, enlarge or expand the existing asset. Examples include adding an extra wing or room to a building or the addition of a lane to an existing roadway. As additions increase service capacity or physical output of a property, they are betterments. The costs of additions should be capitalized. The key consideration is increase of quantity of service or output.

Upgrades

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. An upgrade increases the overall efficiency (i.e. increasing utilization, lowering operating costs, or increasing output of service), quality (i.e. transforms the asset into a higher class property) or extends expected service life of an asset. The costs of upgrades are capitalized. The following examples would have characteristics of an upgrade:

- Installing air conditioning in a building that was previously not air-conditioned increasing the service quality of the property;
- Replacing existing lighting with energy saving lighting reducing future operating costs;
- Substituting a tile roof for wooden shingle increasing the expected useful life of the building beyond its currently estimated life;
- Replacing an elevator with a new high speed elevator improving the building class of the overall property; or
- Replacing a furnace with a high efficiency furnace decreasing future operating costs.

Factors Affecting Asset

Trade In

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 assets being traded in. The new asset acquired is recorded at its full cost; trade in value for the old asset does not affect cost.

Disposal

On disposal of an asset, the historical cost and accumulated amortization must be removed from the books. The disposal shall be documented in a memorandum, e-mail or by invoice. The difference between the net proceeds on disposal and the net book value must be recorded as a gain or a loss for the accounting period.

Write Off

A write off is used to reflect total impairment in the value of an asset. Capital assets are written off in instances where they are destroyed, stolen, lost, sold or obsolete. The write off of an asset requires approval by a properly authorized officer. Any abandoned or indefinitely postponed projects must be written down to their net realizable value and charged to the period in which the abandonment or indefinite postponement occurs.

Amortization

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. The asset will be used to provide services or deliver programs to the public over the assets' estimated useful lives. Where the residual value of the asset is significant then it should be factored into the calculation of amortization otherwise assume zero residual value for the components. 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 the extent to which an asset's service potential is consumed over its useful life.

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. Where construction of an asset is comprised of distinct, multiple and self-contained phases, amortization must begin for the distinct phases that are completed. Various methods of amortization are available, however all amortization done by Central Manitoulin has been done using the straight-line method as a preference.

Straight-Line Method

The straight-line method is the most common and preferred method of amortization and is calculated by dividing an asset's original cost by its estimated life in years yielding a constant annual depreciation amount each year. For example, a building that costs \$3,000,000 has an estimated useful life of 40 years would yield annual depreciation of \$75,000 ($\$3,000,000 / 40$ years).

Definitions

Amortization is an accounting concept in which the recorded cost of an asset is distributed in a systematic and rational manner over its estimated useful life and matches the cost of that asset to the periods in which service is derived from the asset on a straight-line basis. Amortization is normally based on the total cost of the asset less its residual value. It is assumed that the tangible capital asset will be held for an extended period of time and the residual value will be immaterial. The start date will be the first day of the month following the month the asset is placed into service.

Betterment is a material cost incurred to enhance the service potential of an asset and will:

- Increase the previously assessed physical output or service capacity;
- Significantly lower associated operating costs (efficiency);
- Extend the life of the property; or
- Improve the quality of the output.

Contributed assets are capital assets such as developer constructed services in new subdivisions (i.e. water, sewer or roads infrastructure) acquired without cash outlay and will be valued at fair market value when the asset is placed into productive use/service (i.e. upon initial acceptance).

Historical 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.

Maintenance is a recurrent expenditure, periodically or regularly required as part of the anticipated schedule of works required ensuring 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 assessed useful life.

Pooling of assets refers to assets of value below the materiality threshold when considered on an individual basis but collectively make up a significant group of assets that exceeds the threshold level (i.e. computers, valves, hydrants, furniture, water/sewer service laterals and stretchers, etc.).

Residual value is the estimated net realizable value of a tangible capital asset at the end of its useful life.

Tangible capital assets 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;
- Have useful lives extending beyond an accounting period;
- Are intended to be used on a continuing basis; and
- Are not intended for sale in the ordinary course of operations.

Threshold is generally the minimum cost that an individual asset must have before it is to be treated as a tangible capital asset. The threshold amount is to be used as a guide in addition to professional judgement.

Useful life is the period over which an asset will be used. An asset will most likely be removed from service when it is not longer economically viable. Useful and economic lives are synonymous.

Appendices

Capital Thresholds For Asset Categories	
Water & Sewer	\$10,000.00
Machinery & Equipment	\$5,000.00
Vehicles	\$5,000.00
Buildings	\$10,000.00
Road Network	\$10,000.00
Bridges & Main Culverts	\$5,000.00
Pooled Assets (ie. Streetlights, signs, culverts, miscellaneous)	\$5000.00

Appendices Cont'd

Maximum Useful Life Values Used for Amortization			
Asset Category	Useful Life	Amortization	Amortization Calculations
Water & Sewer Assets	40 Years	Straight Line Amortization	[Historical Cost - {(Historical Cost / 40) x Accumulated Life}] = Opening Net Book Value
Vehicles – Fire Trucks	25 Years	Straight Line Amortization	[Historical Cost - {(Historical Cost / 25) x Accumulated Life}] = Opening Net Book Value
Vehicles – Light, Med, Heavy Duty	10 Years	Straight Line Amortization	[Historical Cost - {(Historical Cost / 10) x Accumulated Life}] = Opening Net Book Value
Heavy Construction Equipment	25 Years	Straight Line Amortization	[Historical Cost - {(Historical Cost / 25) x Accumulated Life}] = Opening Net Book Value

Buildings	50 years	Straight Line Amortization	[Historical Cost -{(Historical Cost / 50) x Accumulated Life}] = Opening Net Book Value
Land	Infinite	Not Amortized	Not Amortized
Roads – Surface Treated	20 Years	Straight Line Amortization	[Historical Cost -{(Historical Cost / 20) x Accumulated Life}] = Opening Net Book Value
Roads – Gravel	15 Years	Straight Line Amortization	[Historical Cost -{(Historical Cost / 15) x Accumulated Life}] = Opening Net Book Value
Culverts	30 Years	Straight Line Amortization	[Historical Cost -{(Historical Cost / 30) x Accumulated Life}] = Opening Net Book Value
Road Signs	30 Years	Straight Line Amortization	[Historical Cost -{(Historical Cost / 30) x Accumulated Life}] = Opening Net Book Value
Bridges – Steel	40 years	Straight Line Amortization	[Historical Cost -{(Historical Cost / 40) x Accumulated Life}] = Opening Net Book Value
Bridges – Timber	30 years	Straight Line Amortization	[Historical Cost -{(Historical Cost / 30) x Accumulated Life}] = Opening Net Book Value
Street Lights	30 Years	Straight Line Amortization	[Historical Cost -{(Historical Cost / 30) x Accumulated Life}] = Opening Net Book Value
Office Furniture	20 Years	Straight Line Amortization	[Historical Cost -{(Historical Cost / 20) x Accumulated Life}] = Opening Net Book Value
Audiovisual Equipment	10 Years	Straight Line Amortization	[Historical Cost -{(Historical Cost / 10) x Accumulated Life}] = Opening Net Book Value
Computer Systems	5 years	Straight Line Amortization	[Historical Cost -{(Historical Cost / 5) x Accumulated Life}] = Opening Net Book Value

NOTE: Maximum useful life values used from OMBI Handbook, March 2007